BANKRUPTCY: THE SHOPPING CENTER PROTECTION IMPROVEMENT ACT OF 1982

HEARING

BEFORE THE

SUBCOMMITTEE ON COURTS

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

S. 2297

A BILL TO AMEND TITLE 11, UNITED STATES CODE, TO IMPROVE THE PROTECTIONS FOR SHOPPING CENTERS AND THEIR TENANTS UNDER THE BANKRUPTCY CODE

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BANKRUPTCY: THE SHOPPING CENTER PROTECTION IMPROVEMENT ACT OF 1982

MONDAY, MAY 3, 1982

U.S. SENATE,
SUBCOMMITTEE ON COURTS,
COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9 a.m., in room 2228, Dirksen Senate Office Building, Senator Howell Heflin (acting chairman) presiding.

Staff present: Pete Velde, chief counsel and staff director; Arthur Briskman, minority chief counsel; Pat Brown, chief clerk; Doug Comer, Kevin Manson, Mary B. Troland, Barry Bauman, counsels; Randall Rader, general counsel, Subcommittee on the Constitution; and Jose Zavala, legislative correspondent.

OPENING STATEMENT OF SENATOR HOWELL HEFLIN

Senator HEFLIN. We will call the hearing to order. We will try to expedite the hearing as best we can.

Today, the Senate Judiciary Subcommittee on Courts will hear testimony on Senate bill 2297, the Shopping Center Protection Improvement Act of 1982. I would like to thank my distinguished colleague, Senator Robert Dole, the chairman of this subcommittee, for allowing me the opportunity to conduct these hearings. Senator Dole is an exceptionally busy Senator, being the chairman of the Finance Committee, and he was extremely busy last year with the agricultural bill. Senator Dole has many things on his schedule today, including the Voting Rights Act, where he is trying to work out accords between the various elements pertaining to that bill. So, I am pleased to substitute for him at this hearing.

Senate bill 2297, introduced by Senators Orrin Hatch and Dennis DeConcini, would amend the Bankruptcy Reform Act of 1978 to endeavor to curtail inappropriate disruption of shopping centers and their member tenants in instances where a leasee within that center has requested relief under the Bankrupty Act.

The U.S. Congress has long legislated in the field of bankruptcy. The 13th amendment to the U.S. Constitution, which prohibits involuntary servitude except as a punishment for crime, serves as the basis for protecting the rights of the debtor as well as the creditor. The first extensive Bankruptcy Act was passed by Congress in 1898, and this act has been amended on numerous occasions since that time.

Today, filings for bankruptcies are at their highest level in 40 years. Given this background, it has become increasingly necessary to prevent the adverse ripple effect throughout the economic system which bankruptcies might create.

It has been stated that there is a fragile relationship among the tenants of a shopping center such that the bankruptcy of one tenant has a severe impact on the other tenants. It is this fragile relationship as well as the prevention of business disruption which this legislation attempts to correct and which we will examine today.

Senator Orrin Hatch has an introductory statement on this bill which we will make part of the record in this case.

[The prepared statement of Senator Hatch follows:]

PREPARED STATEMENT OF SENATOR ORRIN G. HATCH

Mr. Chairman, I am delighted to introduce my friend and fellow Utahan, Mr. Wally Woodbury. Before I tell you of my respect for Wally, however, I would like to take this opportunity to thank you, Mr. Chairman, and each of the members of this subcommittee for scheduling this important hearing on my bill, S. 2297.

Shopping center tenants are inextricably tied together. When one suffers financial failure, others may be placed in jeopardy as well if our bankruptcy code does not insure an efficient arrangement to fill the shopping center's vacancy. Prior to 1978 this was accomplished by lease clauses allowing the lessor to regain control of the lease in the event of bankruptcy. The 1978 act made such lease clauses unenforceable. Instead the lease becomes a part of the bankrupt estate. This can create acute problems when the estate's administrator neither assumes or assigns the lease for several months. The surrounding shopping center tenants must bear the extra burden caused by the vacancy—a particularly difficult problem if the shopping center was built around a single major business which has now folded. A single bankruptcy could trigger others. S. 2297 establishes a 60-day time limit for the administrator's decision to assume or reject a lease. This gives an administrator some incentive to either find a new tenant himself or return the lease to the shopping center within a reasonable period of time. The fate of the shopping center will not hang in the balance until the estate is settled.

In addition, the bill addresses a few other problems. In the event the lease is assumed by the administrator, it may be assigned to a business not in compliance with the use limitations of the lease, not of the financial quality required by the center, or which does not pay the customary security deposit. For example, a men's shoe shore may have entered a shopping center lease on the understanding that all men's shoe stores would pay identical rent. Assigning a women's shoe store lease at a lower rent to a fourth men's shoe store would both oversaturate the men's shoe store market and give the fourth store the unfair advantage of a lower overhead. This only illustrates one of the complexities of shopping center bankruptcies. S. 2297 sets reasonable standards to deal with these unique problems.

My deep interest in this area of the law stems largely from my friendship with Wally Woodbury. The subcommittee could not have chosen a more competent witness than Wally. Wally is chairman of the board of the Woodbury Corp., a 60-year-old firm specializing in shopping center development and management. I am confident that his vast experience with precisely the kind of problems this legislation is designed to remedy will benefit the subcommittee greatly.

Once again, I would like to thank the subcommittee for acting expeditiously on a bill that was only introduced just over a month ago. This demonstrates the subcommittee's willingness to forge a workable and fair bankruptcy code.

Senator HEFLIN. I look forward to receiving testimony from outstanding litigators and businessmen on this legislation. Our first witness is Mr. Wallace R. Woodbury, of Woodbury Corp., in Salt Lake City, Utah.

Mr. Woodbury, we welcome you.

STATEMENT OF WALLACE R. WOODBURY, CHAIRMAN, WOODBURY CORP., SALT LAKE CITY, UTAH, REPRESENTING THE INTERNATIONAL COUNCIL OF SHOPPING CENTERS; HOWARD C. OLIVER, SENIOR VICE PRESIDENT, FINANCE AND OPERATIONS, JIM WILSON & ASSOCIATES, INC., MONTGOMERY, ALA.; GEORGE LAMBROSE, MANAGING PARTNER AND OWNER, SOUTHGATE MALL, MISSOULA, MONT.; AND JOHN S. HOLMES, SR., PRESIDENT, FREDERICK SHOPPING CENTER MERCHANTS ASSOCIATION, FREDERICK, MD.

Mr. WOODBURY. Thank you, Mr. Chairman.

My name has already been given by the chairman, Wallace R. Woodbury. I am from Woodbury Corp., a real estate development brokerage and management firm, headquartered in Salt Lake City. We are active in the development and management of all sizes of shopping centers as well as other commercial, industrial, and office buildings. I am also a member of the government affairs committee of the International Council of Shopping Centers, and I am here testifying on my own behalf and on behalf of my firm, and also giving the testimony of the International Council of Shopping Centers.

We have enclosed with our testimony an extensive analysis of the side-by-side language of the bill, Mr. Chairman, and some summaries of the effects of the various things that we are going to talk about in much greater detail than we will have time to mention in our oral statement. I am obviously testifying in support of Senate bill 2297. We feel rather strongly that contrary to the expressed congressional intent in the 1978 act, the administration and certain ambiguities in the act have resulted in depriving the landlord and certain of the nonbankrupt tenants from adequate remedies in the actual administration of the bankruptcy laws as far as they apply to shopping centers.

A shopping center is a combination of retailers, each dependent upon the other to attract shoppers to an especially designed structure intended to facilitate and encourage shopping. As a result of such a relationship, the bankruptcy of one tenant often has a serious impact on the other tenants. In a sense, a shopping center is a department store, and each tenant in a properly planned tenant mix is one of the departments in that department store. And any unreasonable interference with the balance of departments in that store or in that shopping center creates an outbalance that does damage to everyone. A successful shopping center is typically the result of sophisticated planning and a very delicate balance of merchants. Tenants are chosen on the basis of their business image and use, an analysis and evaluation of the market demands of the area, and an examination of the financial capacity and business experience of the particular tenant in relation to the potential customers to be served. A well-planned project with a balanced mix of stores maximizes the potential benefits to the landlord and tenants as well as to the community served.

Shopping center leases are made on a long-term basis, considering the large investment usually made by tenants in preparing their establishments for the contemplated business. These long-term lease arrangements, which are granted to tenants for specific

and limited uses of the landlord's property for very long periods of time, put the landlord into a position unlike that of a merchandise creditor or financial institutional lender. Such suppliers or lenders can make periodic, short-term reviews of the financial condition of their customers, and can freely terminate credit when they feel the customer's capacity to pay has been impaired. A landlord, under a long-term agreement, does not have that flexibility. Shopping center leases usually contain very strict limitations on use; affirmative covenants relating to radius clauses, forbidding the dilution of tenant market potential; prohibitions on assignment, unless the landlord is satisfied with the financial stability, credit, public image and intended use of the potential assignee; and specific requirements for cooperative advertising, promotion, common area use and maintenance, sign control, and uniform hours of operation.

The vacancy of any tenant space for an extended period of time can seriously disrupt not only the neighboring tenants, but the entire shopping center. Customer traffic is reduced not only by the decreased supply of products or services, but also by the less pleasant atmosphere resulting from boarding up a portion of a shopping center. Where the vacant space is that of an anchor store, the effect on the shopping center and its other tenants can be devastating.

The International Council of Shopping Centers is an association of some 10,000 members, composed of both developers and retailers, in addition to some architects and others who are involved in putting the packages together. As a result, it is an association of people that have a common goal to achieve—success for the center.

The assignment of a lease to a tenant in the same business as other existing tenants might substantially reduce the revenue of these tenants, thereby jeopardizing their solvency and affecting their ability to pay rent. In addition, the amount of guaranteed minimum rent and percentage rental rates paid by shopping center tenants is, in most instances, dependent upon the type of business of the particular tenant, and some businesses traditionally pay higher square footage rentals and have higher percentage rentals than tenants operating other businesses.

Now, if I were a landlord owning a freestanding building somewhere, I would probably want to rent it for the greatest rent obtainable. In leasing a shopping center, we sacrifice higher rents to get this delicate balance of tenant mix. We know that certain types of stores just do not pay as much rent. But in order to achieve that balance, we sacrifice highest rent in order to get an overall department-store-effective operating unit.

The assignment of a lease to a tenant in a business other than that of the assignor could give the assignee an unfair advantage over existing tenants in the same business who are paying the higher rental rates consistent with the nature of their businesses. Also, the percentage rates paid by different types of tenants are different, and to assign the lease without any modification of the percentage clause would be unfair to existing tenants in competing businesses.

Prior to the enactment of the Bankruptcy Reform Act of 1978, the shopping center owner could protect the rights and interests of other tenants in the shopping center by enforcing contractual lease

provisions permitting the termination or restricting the assignment or other disposition of the lease in case of bankruptcy. Under the code, such provisions became unenforceable, and the fate of the lease came under the control of the trustee of a bankrupt tenant. Such trustees are granted considerable discretion under the code, particularly in chapter 11 proceedings. However, Congress recognized the special problems of shopping centers by enacting special provisions in sections 365 (b)(1)(C) and (b)(3), specifying criteria which the trustee is required to meet in order to affirm or assign an unexpired lease of the debtor.

Unfortunately, however, in actual practice the specification of such criteria has not proved adequate to provide the kinds of protection that Congress intended. For instance, one of the most oppressive problems faced by shopping centers results from the failure of the code to require the trustee to accept or reject the unexpired lease within a specified time limit in a nonliquidation type bankruptcy proceeding. Also, there is no time limit specified requiring the trustee even to release jurisdiction over an unwanted leasehold, or even an expired lease, to allow the landlord to recover possession even where the tenant is holding sufferance only and really has no legal right to be there.

Some trustees refuse to recommend release of the premises even where they know full well that there is no interest of the tenant to be preserved for the bankruptcy estate. In the meantime, the landlord may not rerent the premises or prosecute any action to recover possession because all State court proceedings are stayed. Other nonbankrupt tenants are usually damaged by this vacancy. On some occasions, even where the trustee has recommended that the property be released to the landlord because there is no value to be preserved for the bankruptcy estate, the court rejects the recommendation or, more often, merely avoids making any decision. For example, in two cases where Hermes Associates—that happens to be a Utah firm—operates two shopping centers known as the Family Center in Las Vegas, Nev., they lease to a California-based tenant known as Brandalls. The tenant filed for bankruptcy under chapter 11 on March 16, 1981. Rents were paid through 1980.

The trustee recommended to the court that the vacant leasehold interest resulting from the bankrupt moving from the premises be surrendered to the landlord, because they had no idea where they would find tenants. There was a surplus of space available. Nonetheless, the California court refused to take any action, and in order to even pursue an action to recover possession, the landlord finally, by paying $2,000 to the California court, was able to get them to take the action to honor the request of the trustee. After such payment, possession was finally surrendered to the landlord in July, and new tenants were finally located in October. The landlord received no rental from January through September. In another case, in Ogden, Utah, we had leased a space to Odyssey Records & Tapes, a California-headquartered company.

Senator HEFLIN. I have read your statement, so, if you will, summarize it.

Mr. WOODBURY. All right.

Senator HEFLIN. We are making a record for those that are not here, so if you would, try to summarize it.

Mr. WOODBURY. Well, in this case of Odyssey Records, we leased the space to Odyssey Records. They exercised their renewal option and then, just a few days afterward, filed chapter 11 proceedings. We had a replacement tenant. They had closed their doors.

The bankruptcy court in California rejected our request for a release, and rather leased the premises to an entity that agreed to buy a number of these stores that had a practice of merely forming shell corporations to run each store—go in and run going-out-of-business sales and this type of situation, and then default on leases. That is what happened here. They went in and then departed from the use clause and commenced running a business identical to the next-door tenant that was a very important tenant to us. Ultimately, the tenant quit because they felt we had violated our covenants to them. After 14 months, the replacement tenant went out of business and left us holding the bag for about 3 months' rent.

Now, I will not go into these other cases that are in my testimony, except to suggest that these are examples of the types of situations that would be cured by the language of Senate bill 2297. It would provide reasonable protection to the landlord and the nonbankrupt remaining tenants of a shopping center from the extended delays and losses resulting from the bankruptcy of other tenants in the shopping center. Where good cause exists, the court would still have the right to extend the time periods that have been specified.

Thank you very much, Mr. Chairman.

Senator HEFLIN. Mr. Woodbury, I reckon anyone traveling throughout the country today will see that there are a large number of small store vacancies in many local shopping centers. Do landlords account and plan for a certain amount of vacancies, whether they are due to bankruptcy or other reasons?

Mr. WOODBURY. Well, we certainly hope for no vacancies because vacancies do damage the other tenants. Sometimes, when you are building a center in the first instance, you are not totally preleased, so you do not know for sure. But it is your contemplation that certain types of tenants blend one with another, and that those types of tenants should be in the center because they have a symbiotic effect one upon the other. We have the good fortune of having very few vacancies in our shopping centers.

Senator HEFLIN. We have witnessed over the last several decades the slow demise of downtown urban areas. Certainly, the ripple effect is much the same in a shopping center where certain stores become vacant. Why should tenants be given special legislative treatment in shopping centers in bankruptcy proceedings, as opposed to other areas?

Mr. WOODBURY. Well, if you have freestanding stores, it is not really a question of where they are located. I have a downtown shopping center in Ogden, Utah, along with Ernie Haun, and that is a planned unit deal.

Where you have freestanding stores, your motivation is to go out and get the highest rent. When you have a group of stores and you are trying to run them as, if you please, departments of one operation, then you have a delicate balance that has to be maintained. You rent to a software store, a clothing store, for maybe half the rental rate that you do to a jewelry store, and this type of thing.

So, you have sacrificed rental rate to achieve a balance of success that helps each of the tenants succeed, and you do not have that situation in a downtown situation because of the lack of unified planning.

Senator HEFLIN. That comes down, basically, to the words "quality control."

Mr. WOODBURY. I think it does, yes, sir.

Senator HEFLIN. We hear this argument in Congress frequently, in order to operate something differently or to authorize a franchise—the words "quality control." I did not do a very good job of convincing them that quality control in the growing of peanuts was an essential part of it in regard to allotments and to special treatment being given.

But the issue for any special treatment is basically that it protects quality control. Is that the general, overall philosophy?

Mr. WOODBURY. I think it definitely does protect quality control. I think, also, that in the 1978 act, Congress recognized that distinction between shopping centers. The request that we are making in this bill merely tries to bring about the very purposes that were already expressed in the 1978 act, but because of a couple of ambiguities and certain lack of time, limits on making decisions have created problems for us. So, it does not really represent a change in substance from the present intent of Congress.

Senator HEFLIN. All right, sir, thank you.

Our next witness is Mr. Howard C. Oliver, of Jim Wilson & Associates in Montgomery. I have known Mr. Oliver for a number of years—a very brilliant scholar in law school. He has been a very capable attorney practicing with Hobbs, Copeland, Screws & Franco in Montgomery, and now is in the shopping center business. The shopping center business must be lucrative, Mr. Oliver, to attract you from your very lucrative law practice. But we are pleased to see you and hear you testify at this time.

Mr. OLIVER. Thank you very much, Senator. I appreciate the opportunity. I am afraid it is not as lucrative as it was a couple of years ago, however. Maybe we can get a little lower interest rate and we will all be better off.

Senator HEFLIN. I thought you were going to blame it all on the Bankruptcy Act of 1978. [Laughter.]

Mr. OLIVER. No, sir, but it has not helped any.

I am not appearing today as a lawyer and do not purport to be an expert on the bankruptcy law, but in my present job I have responsibility for running all of our properties, and that is 12 regional malls and 5 strip centers from North Carolina to Florida to Texas.

I will depart from my written statement and just briefly summarize what I have to say. There are three real problems that I have run into and continue to run into. The first I could characterize as delay. What happens is 99 percent of the time, you have already had problems with the tenant before. He is 3 or 4 months behind in the rent; he may have already vacated the premises and be gone for months. And you are trying to terminate the lease all that time and then he goes into bankruptcy, which simply means another 4 to 6 months' delay.

It is almost as if the delay is an asset of the estate, because what you run into usually is the first thing the trustee does, even if he does not want the premises, will be to come to you and say, "Now, you can buy your way out of this lease if you want your premises back in a reasonable period of time." You are faced with just a built-in, inherent delay because there is no fixed-time-period requirement to accept or reject the lease.

That is unfair, I think, to the landlord, and it also conceivably could present a very bad problem to the small tenants, Senator, because our experience has been that if you have got a big tenant that closes its doors—an anchor store or something along these lines—the effect is really traumatic on the small tenants who are located close to it.

We have the Sunrise Mall in Corpus Christi, Tex., that is probably one of the most successful retail properties that opened in 1981, and one of the department stores was late opening. It was not a bankruptcy; it was simply that they were late. But of the 4 problem tenants out of 102, 3 of them were right up next to that store.

In a bankruptcy situation, the inability to get that space back to keep the property viable can be a real, real hardship on the small tenants, especially local tenants. The national chains have enough financial resources where they can hang on for 9 months, 1 year, or whatever delay is built in. But a small mom-and-pop operation really has tremendous financial hardship.

The second point is that this delay has a certain amount of cost incident to it. We find that we start out being a fairly large general creditor; when they go into bankruptcy, we have to continue sometimes to provide services, and so forth, for the store, and we are faced with generally receiving very little for the space during the period, especially with tenants who ultimately reject the lease and move on and are not successful working out of the bankruptcy.

One of the biggest problems, and a third one, would be the assignment to a successor of this bankrupt tenant. Here, the trustee has one interest and one interest only. He is interested in making a buck for the estate. He could care less if what he does is not in the best interests of other tenants in the center or the landlord.

We had a recent incident where we had a mall in Florida, and we have got about 50 stores. It was, you know, popular-priced ladies wear. Well, in our judgment—and I think it is a reasonable judgment and one that is sound—that is as many popular-priced ladies stores as you need in a mall that size; you just do not need anymore.

Well, that was the highest price the trustee could get for that space, so he wanted to lease it to a third one. Now, these two people did not have a voice in the matter; they had no standing, really, to come to court and say, "Hey, we do not need a third store in here." It really would not hurt the landlord that much in this particular instance, but the two other stores it damaged very much. So, this is a very common happening.

In a well-planned shopping center, an awful lot of work and effort go into trying to get it right, and it is most disappointing to the landlord and to the tenants to wake up and find that, in total contravention to a lease provision, a lease is going to be assigned to the highest bidder, because there is not a space in a shopping

center that is 1 year old that I cannot rent for more dollars if I do not care about whom I rent it to—not a one.

So, these are the three things that particularly have been a problem to us, and we appreciate the opportunity to express our problems to the committee and would hope that they would act favorably on our problems and requests in this bill.

Senator HEFLIN. Let me ask you this. We will say that there is a store in a shopping center that is getting into trouble. What is generally the history? They are in default prior to going into bankruptcy, probably, for how many months in the payment of rent prior to the filing of bankruptcy?

Mr. OLIVER. Three or four months.

Senator HEFLIN. And in your contractual relationship with that to-be-bankrupt tenant, I suppose you have got some sort of deposit lien provision on their personal property within the lien provisions over personal property within the store. Is there a history, though, of removing personal property from it when they do go into bankruptcy?

Mr. OLIVER. Yes, sir, that is very true. We find that that is not very much protection. We very seldom have very much of a lien. Often, the tenant has financed everything with a bank or some other financial institution and the landlord has subordinated all of his liens to that institution.

Senator HEFLIN. In other words, the shopping center landlord generally is required to have to subordinate his common-law lien?

Mr. OLIVER. He is not normally required to, but with an undercapitalized tenant, if you want the tenant, you have to give some. So, that is just simply a fact of life. With smaller tenants, lack of capitalization is one of the primary reasons for bankruptcies, and it is very usual to find that you have subordinated, and so forth. If you have not subordinated, he moved out in the middle of the night and moved it out with him, a lot of times.

Senator HEFLIN. What is your normal requirement for advanced deposit on rent? What do you require, a couple of months?

Mr. OLIVER. No, sir. In the mall I was just speaking of in Texas, we had occasion to sell it a couple of days ago and we had zero security deposit. Today, in shopping centers, it will vary certainly, but we normally have zero.

Senator HEFLIN. Well what is the timeframe on the failure of the trustee to make a decision before you can start drawing in rent? Is it generally from the bankruptcy filing until the trustee makes some decision and you are put back into a rent-drawing posture?

Mr. OLIVER. Well, you get 3 months, then he goes bankrupt, then if you really have a good set of lawyers and you spend a fair amount of money and try diligently, about 4 or 5 months would be——

Senator HEFLIN. I suppose that will vary. You will have some referees in bankruptcy or trustees that are just burdened with a great number of bankruptcies.

Mr. OLIVER. Yes, sir.

Senator HEFLIN. Do you know how far that has extended? Has it gone as far as 1 year?

Mr. OLIVER. Well, I have not had that experience, but I have one that has been going on for 6 months right now. So, I can let you

know if we ever get out of it. The thing is that if the lease is rejected after 6 months, only then can you really start leasing it to the next guy. So, it is going to sit vacant for another 3 or 4 months while you get another tenant in there, and so forth, because until you know whether you have the premises or not, you cannot go out and spend the money to bring people down and to show them the premises, and so forth. They do not want to spend the time on something that they may never have the opportunity to use. So, it is just in limbo for an extended period of time, to the landlord's detriment and, in many instances, to smaller tenants' detriment.

Senator HEFLIN. Then, if you have got 4 or 5 months where there has been a failure to pay prior to bankruptcy, and then you have got 4 months pertaining to decisionmaking and the normal procedures before you are released to then go ahead and get another tenant in there to draw rent, you have got 8 to 10 months, anyway, in the normal bankruptcy in which there is a loss of rent.

Mr. OLIVER. Yes, sir, it could easily be that much.

Senator HEFLIN. The provisions in the bill would allow for immediate decisionmaking on the part of the trustee or the debtor in possession to free it and to allow the landlord to be able to choose a tenant.

Mr. OLIVER. Yes, sir.

Senator HEFLIN. Now, your provisions say if they do not, there is, in effect, a right to collect the rents during a certain period of time?

Mr. OLIVER. Yes, sir.

Senator HEFLIN. Now, your assignment is a delicate situation by which every part comes together in a shopping center, and you can have undue competition, I guess you would say—or undue, untimely, or unwise use of the space. How does the bill attempt to correct this?

Mr. OLIVER. I think it provides that if there is a specific use provided for in the lease, it will be complied with, where there is a substantial sort of tenant mix formula under the existing law. But in a mall with 50 or 60 tenants, it is virtually impossible for a landlord—and he is the only one with a voice in the matter—to come in and say that one store has any substantial effect, period.

In other words, the courts, in our experience, and the trustees pretty well take the position that one tenant just really does not make any difference. Well, we feel it really does make a difference. We would not have bargained for that in the lease to begin with if we did not think it was important.

There are a great many examples which we could get into where that is very important. When you have 50 or 60 tenants, you only need 1 record store. If you put two record stores in there, you will have two unsuccessful operations. We run into the situation where if somebody can make a quick buck to rent it to the second record store, he is going to try to rent it to the second record store. He will rent it to anybody; he could care less about what the next use is. His sole interest is increasing the estate of the bankrupt.

Senator HEFLIN. In your basic agreements in a shopping center, are there covenants between landlords and tenants? Are the shopping center agreements basically with cross-covenants from tenant to tenant?

Mr. OLIVER. No, sir.

Senator HEFLIN. I just wondered, in other words, if there was a basic document in your contractual arrangement by which each tenant, in effect, agreed to certain basic covenants that were mutual covenants existing between tenants and made part of a contract, could the courts enforce those covenants?

Let us say that there might be a failure of this remedial legislation to pass. Contractually, could you arrange it such that courts would have a right to equitably enforce covenants even with a bankruptcy procedure involved?

Mr. OLIVER. Senator, I might want to hold that for the lawyers and let them handle that. I am not sure.

Senator HEFLIN. I am not really sure whether a bankrupt trustee or referee would have a right to violate existing cross-covenants between tenants as well as with the landlord. That might be subject to 40 years of practice before it gets to a 5-to-4 decision in the U.S. Supreme Court, so I suppose you are hunting more of an immediate remedy for that situation.

Well, thank you, Mr. Oliver; we appreciate your testimony. Our next witness is Mr. George Lambrose, of Lambrose Realty in Montana. I have a statement here from Senator Max Baucus, who has requested that it be read in full.

[The prepared statement of Senator Baucus follows:]

PREPARED STATEMENT OF SENATOR MAX BAUCUS

Mr. Chairman, I regret that previous commitments prevent me from participating in today's hearing. Bankruptcy reform in general and its impact on shopping centers are issues of interest to me. I commend the chairman for his leadership in bringing these issues to the attention of the committee and for expediting their consideration.

I am particularly sorry that I will not be able to personally introduce to the committee George Lambrose of Missoula, Mont. George is an excellent Montanan and a very successful businessman. His direct, firsthand experience with the operation of shopping centers makes him uniquely qualified to appear before this committee. I know he will make a significant contribution to the hearing record and that the entire committee will greatly benefit from his participation. I know that the committee will extend every courtesy to George in my absence.

Again, I regret I am unable to participate personally in today's hearings. However, please know that I will take great interest in this legislation as it progresses through the committee and the Senate. Please extend to the committee and to George Lambrose my appreciation for their commitment and interest in this important legislative matter.

Senator HEFLIN. Mr. Lambrose, we would be delighted to hear from you at this time.

Mr. LAMBROSE. Thank you, Mr. Heflin. I am testifying this morning in support of S. 2297 because this bill would remedy problems created by the Bankruptcy Reform Act of 1978. These problems are serious and have already damaged the business of many shopping centers and many more tenants.

One of the changes which this bill would make would be to delete the word "substantially" from provisions of the code which require that the trustee or debtor in possession make assurances regarding conformance with the use clause of lease and disruption of shopping center tenant mix.

The need for this change is, at the same time, extremely important and somewhat difficult to explain. Since other witnesses this

morning will be testifying regarding the other provisions of this proposal, I will confine my comments to this one issue.

I will depart from the text and bring attention to the subcommittee of the tenant mix evaluation sheet which I have accompanied as an exhibit to my written remarks. I would like to have you review those tenant mix categories which will illustrate the importance of the balance of the tenant mix that has been discussed so far this morning.

I am probably the least experienced of the panel here; I am only involved with one shopping center in one small community in Montana. We have 4 department stores and 92 tenants, so it is a substantial retail facility in our community.

As such, there is no national rage to get into this shopping center as far as being an area where substantial numbers of tenants are available. We were fortunate when we opened our mall that the mall opened up 100 percent occupied and gave all of the tenants at that time a greater opportunity to develop a benefit to their retail sales rather than the normal buildup and the balance of a tenant mix. So, we had the textbook solution on how tenant mix would probably be best effected for the users in the mall.

At the present time, our community has about a 14-percent unemployment rate, and when a retail facility such as this is involved in an unemployment rate area like ours, there is a very fragile line of possible tenant losses. Because of their borrowing at the very high interest rates and the very difficulty of remaining in business, the tenant mix becomes very sensitive.

We have, for example, three stores of a category in our mall that are presently under very, very sensitive negotiations with me in order to prevent their loss of business and the loss of substantial amounts of funds that they have invested in the shopping center to first become part of the shopping center.

If, on the one hand, I were to ignore their special requests, these people would probably already not be in business in the mall. So, we have a very close relationship. However, it is one of the categories that, nationally speaking, a tenant might wish to become part of the center in that same category. If a bankrupt judge were to decide that this was the best dollar value that he could receive from a substitute tenant, I believe that this would disrupt the three tenants very sensitively and cause irreperable harm to the tenant that is in the category that might not be judged so by a bankruptcy judge.

It is important to note that deleting the word "substantially" from these provisions would in no way prevent the assignment of debtors of their leases. Although shopping center lease use provisions are drawn with various degrees of specificity, even the narrowest use description still covers market segments served by a very large number of existing and potential businesses.

In conclusion, I urge the subcommittee to approve Senate bill 2297, and I hope this legislation will be enacted into law soon. Each of the proposals in that bill is needed by shopping centers and their tenants. One of the most important of these changes would be to require that the use clauses in shopping center leases be precisely adhered to and that no disruptions of shopping center mixes occur.

Thank you for consideration of my views.

Senator HEFLIN. Thank you, sir. I do have a question I want to ask. What steps other than amending the bankruptcy laws might a landlord take to contain the adverse ripple effect after a major tenant goes into bankruptcy?

Mr. LAMBROSE. My own experience was in one case of a bankruptcy. I found that in all cases of the bankruptcy that was involved, there was great cooperation between the judge and the attorneys that were involved. It was a case that was pending about 6 months. I had the feeling it was coming; I was trying to be helpful as far as guiding the tenant.

Once it got into bankruptcy, there was an understanding on the part of the judge. What some of the gentlemen have experienced is a bankrupt judge tying this entire space up without any consideration to the people involved. Because of the willingness and the cooperation and the knowledge that I had in working with the tenants, I very quickly was able to get an assignment of the lease and a user of the same quality and the same use to take over the space.

We were able to help the banking facility that was involved in the loan to the tenant. We were able to get the personal guarantees from the debtors involved, and because of the cooperative nature, this all happened in very smooth action. But it took 4 months after the bankruptcy to have a replacement tenant for the particular space. I already had a tenant to take an assignment who was willing to continue that same use.

Senator HEFLIN. Thank you, sir.

Our next witness is Mr. John Holmes, Sr., president of the Merchants Association of Frederick, Md.

Mr. HOLMES. Thank you, Senator. I am president of the Merchants Association in the Frederick Shopping Center, located in Frederick, Md. I own a store in the shopping center which sells delicatessen foods and beverages.

The Frederick Shopping Center is enclosed in a strip center of approximately 25 stores. Most of the businesses are locally owned and family operated. I have operated my store in the shopping center for 22 years. I have been president of the Merchants Association for 11 of those years, and in all that time, really, the most serious problem for our shopping center has been the two stores that they have closed down for bankruptcy.

The purpose of my testimony this morning is to explain the damage to the other tenants in the shopping center, to quickly release the space to operating businesses, and to urge the approval of S. 2297 which would lessen these problems in the future.

A major store in the Frederick Shopping Center was the Food Fair grocery store. This store was centrally located in the shopping center and provided primary drawing power to all the other tenants in the center. On July 31, 1981, the Food Fair store in the Frederick Shopping Center closed. In September 1981, Food Fair assigned its lease to another grocery store, Farm Fresh. Farm Fresh opened for business on November 18.

On July 30, 1981, another store in the center, Joe the Motorist, which was an auto parts and service store, had closed. After unsuccessfully trying to assign its lease for several months, it finally rejected its lease in March. It was not until April that another

tenant was located and operations were resumed in that location—almost 1 year later.

In the case of the Joe the Motorist store, the shopping center tried again to control the lease so that the space could be re-leased to an operating business, but was unable to do so. I had several phone calls myself from Philadelphia from a chain store—Penn Jersey, I believe it is—and they had been in my store many, many times talking about it and were not able to obtain a re-lease from Rosenfeld Realty, which is my landlord.

It was fortunate that the Food Fair succeeded in assigning its lease to another grocery store approximately 2 months after closing. Last week, knowing this bill was coming up, I went down through my shopping center and I talked to many of my merchants, refreshing myself as to the problems that they had. Also, each month we have a merchants meeting; we talk about the problems in the center. So, I am well in tune with what my family's problems are in our center.

If I may leave my message here, I would like to go down some of the stores that are in my center so I can familiarize you with what my center looks like. My center is a strip shopping center. Trible's is a store that sells parts for refrigerators, stoves, and large appliances. We have a Little Professor Bookstore; we have a barbershop; we have a May's Hardware.

All these stores that I am telling you about now are ma-and-pa stores, and father-son, as my store is. I will let you know the balance of the stores that are chain-operated stores.

The Little Professor is a man and wife doing a super job. When the bankruptcy started, it was very, very slow; their traffic flow dropped down to almost half.

Senator HEFLIN. What does the Little Professor sell?

Mr. HOLMES. The Little Professor was very upset because he had a lot of books that he wanted people to read. They lost about 50 percent in traffic, sir.

The barbershop is a family operation, man and wife, and I would say 80 percent of my people here keep a customer count so they know how many people come into their stores since the bankruptcies, and even before that, but they could pick up the percentages there.

The hardware store was down about 20 percent. Bill's Hobby Shop was down about 18 percent. The laundromat had slowed down considerably; he could not give me a figure on it. We have a gas station out front that is a father-son, mother-daughter team that sells gas and does a tremendous job on repairs. They said they were down about 18 percent, and a lot of their customers have not returned since the opening of the two stores.

The Rob Ellen Card Shop sells Hallmark cards. We have a dentist and an optician. He said his business had dropped off, and he has businesses in other locations; the man goes from one store to the other. There is a bridal shop and a ladies hair stylist; they had to lay one girl off.

There is an insurance company; one man owns it, but rents it. Nationwide is in there. We have a deli, which happens to be my shop. Kilbey's Appliance Center sells small appliances and repairs all of their appliances. His appliance center sales had dropped to

almost nothing; the repair business stayed the same. It was not the man; the man is a good man and is a hard worker.

The dry cleaners dropped about 18 percent. C&P Telephone did not notice too much in the traffic. Next are the chain-operated stores. People's Drug Store's traffic count was down 20 percent. Woolworth's was very slow; we could not get any figures. High's was down; the traffic count was very slow. Melart's Jewelry Store was down 40 percent. AAA noted no problems.

Senator HEFLIN. In what period of time did this occur?

Mr. HOLMES. Senator, this started about the middle of July when Food Fair was advertising that they were closing down. The sales started; after the first week, there was no fresh produce or meat. The only thing you had left after the first week was a few cans and things like that, because they were running 20 and 30 percent sales.

Senator HEFLIN. That was July 1981?

Mr. HOLMES. To November 18.

Senator HEFLIN. You feel that all of this is due to the Food Fair and Joe the Motorist being closed down?

Mr. HOLMES. The Food Fair is a major draw. This is what really brings the center together. We have a variety of people which make a well-knit family; we can help ourselves. Customers come into my store and I send them over to the bookstore. We talk about each other, and everyone in our center works well with everybody else in our center.

This has been a successful center up until this time, and I will say one thing. In the last 5 years, we have not had any vacancies in our center. It is a strongly knit group. You go out and you talk with your customers and you find out what they want; you just do not hope that they are going to find what they want in all of our stores. All the managers are good workers.

We have AAA's, the Woolco, and the Horn & Horn Restaurant. They were down about 18 percent; this is a restaurant that is not high priced. Dinners are $4.50, $5.50, $6.50; good food. This was down. Traffic was down.

Senator HEFLIN. What is the unemployment rate in Frederick?

Mr. HOLMES. About 7.2, sir.

Senator HEFLIN. That would be below the national average during that timeframe, would it not?

Mr. HOLMES. We have been very fortunate in our area.

Senator HEFLIN. Well, you are discounting the economy.

Mr. HOLMES. The economy has nothing——

Senator HEFLIN. It is strictly Joe the Motorist and Food Fair that caused this drop in customer traffic?

Mr. HOLMES. If these two stores would have been in there, these people would have done a percentage above, not below. The economy had nothing to do with these people. These were all strong and had been in there a long time; they are strong operators.

Senator HEFLIN. In the center, was there another store similar to Food Fair?

Mr. HOLMES. No. There was only the Food Fair in our shopping center, sir.

Senator HEFLIN. Some shopping centers have two types of stores like that.

Mr. HOLMES. Big stores.

Senator HEFLIN. They compete with each other.

Mr. HOLMES. I wanted to comment on a point that you brought up. Do the landlord and tenant have in the leases a provision that they will not put another shoe store in there or another drug store?

With our landlord, it was a handshake. We are country boys from Frederick and we believe in a handshake. When a guy says he is going to do something, this is what it is going to be.

Senator HEFLIN. In many shopping centers, they take care of accelerated depreciation at early stages. There is a very frequent change of ownership.

Mr. HOLMES. This has not been a change.

Senator HEFLIN. How long has your shopping center been there?

Mr. HOLMES. Our shopping center started in 1957. It has been very successful. The tenant association has been very strong. We have had good response from the neighborhood. We do a lot of community work with everybody in the area. We have good rapport with our town fathers.

We were the first center to come to Frederick, and we now have four large centers and we still are very successful and still full. Food Fair has been replaced with Farm Fresh, and Joe the Motorist has now been replaced with a large store which should be very successful in our center.

Senator HEFLIN. How long did it take to do that?

Mr. HOLMES. Redoing the store, sir?

Senator HEFLIN. No; the replacement.

Mr. HOLMES. Well, the Joe the Motorist store was out from July 30 of last year to April 22 of when they put a man in. That is 9 months; that is a long time. I will say this: when they go bankrupt and they lock that door and the sheriff comes by, the landlord cannot get in. He was not able to get a key, and it happened to be right next to my store.

When they pulled all the things out at 4 in the morning to take them to another store to run their sale, the store was a mess. It took them almost a week to clean up boxes and stuff. I really feel sorry for the landlord with the money he has to spend. They had two fellows come in and put an appraisal on it, and it was over $100,000 to redo the store.

Senator HEFLIN. How long did Food Fair take to get its replacement?

Mr. HOLMES. I would say probably the first of November, we knew which store might have it. They had three other stores applying for it. When I say "they," I mean the Rosenfeld family had someone to take it right over, but they could not.

Senator HEFLIN. When did it open?

Mr. HOLMES. It opened the 18th.

Senator HEFLIN. When did it go into bankruptcy, in July?

Mr. HOLMES. July 18, and they went in on November 18.

Senator HEFLIN. And when did the new store open?

Mr. HOLMES. The 18th of November, sir; it was just about 2 months. They were lucky because another food chain came right on in. They had to do some renovation and some work on it. They do not recover right away, Senator. When they put the stores in, it takes a couple of months to bring customers back. Customers do

drift to other locations, and once they get settled in for 60 days, we have a problem getting our people back and doing business with us.

Senator HEFLIN. What about Joe the Motorist?

Mr. HOLMES. Totally out of business.

Senator HEFLIN. Totally out of business. What is the relationship of cause and effect that Joe the Motorist had upon other tenants? I can see Food Fair being the only substantial food outlet, but would Joe the Motorist have had an effect on——

Mr. HOLMES. When Joe the Motorist opened up in our center in 1957, they had a full line of automotive parts; they sold fishing licenses. They had a three-bay repair shop in the back and they were busy all the time. They had two servicemen working in the bays doing tire work, mufflers, starters, generators. So, they were very, very busy.

Senator HEFLIN. Was there a competitor of his in the center?

Mr. HOLMES. Would he be a competitor?

Senator HEFLIN. No. Was there a competitor prior to his bankruptcy in the center?

Mr. HOLMES. No, sir.

Senator HEFLIN. He was the only one, in effect?

Mr. HOLMES. Right.

Senator HEFLIN. Now, the people that had mufflers installed and everything else, did they usually wait while he did the repairs?

Mr. HOLMES. Some did. A lot of people would go by in the morning and drop their cars off. There would be many cars during the day that would come by—the ladies, the wives. It was sort of a mixed clientele, you might say, that came in to Joe's. Fridays and Saturdays, there were weekend mechanics, and they were very busy on the weekends.

Senator HEFLIN. Well, would those that did come in wander into the shopping center?

Mr. HOLMES. Yes, yes.

Senator HEFLIN. Spending their husbands' money?

Mr. HOLMES. God bless them.

Senator HEFLIN. God bless them? [Laughter.]

Mr. HOLMES. God bless them.

Senator HEFLIN. We have different perspectives. [Laughter.]

Mr. HOLMES. Now, it depends on if the wife is doing the work and the husband is doing the carousing.

Senator HEFLIN. Well, my wife will not let me go to a grocery store. She says I waste money and buy all the diet foods that never are used.

Do you want to add anything else?

Mr. HOLMES. I think you have read my statement. My point is that we need to shorten the time of bankruptcies. We should give the landlord a chance to be able to negotiate and bring in the people that are going to be able to help the center in its entirety. This is what I have seen in the many years that I have been president of the association in Frederick. I feel my association and my shopping center is not the only one; all the other presidents must feel the same pressures from the people in the center.

Senator HEFLIN. Let me ask this if any one of the panel members that wants to answer it, because we read statistics which would in-

dicate that half of all the retail trade is now being conducted in shopping centers throughout the United States.

Are there any indications that there is more economic loss resulting from individual bankruptcies to shopping centers as opposed to areas that are not under a shopping center—we will say a downtown area?

There may be no studies or statistics made, but we will just say that a nonshopping center approach which is an intensified business area that has numerous types of businesses—are there any indications that bankruptices are causing shopping centers more losses than those that are not in shopping centers, but in intensified retail neighborhoods?

Mr. HOLMES. Senator, I would like to bring this in with that point. In another 3 months, Kilbey's Appliance Center would have been out of business because of this.

Mr. LAMBROSE. Senator, we had an experience in one of those small malls in Montana which was supported by the problem that with one bankruptcy, that triggered another, and a mall that was practically full 3 months ago is on the verge of being 30 percent empty because of the fear of the domino effect of not being in the center with the related attraction.

Mr. WOODBURY. We find that type of thing, Senator. Actually, 20 percent of the shopping centers are in downtowns. So, it really is not a question of urban or rural, but it is that planned balance and that balanced mix that does not exist with a freestanding location where each is a law unto himself. So, there are other people involved than the developer in the shopping center situation; it has more of a symbiotic effect on other tenants that are there.

Senator HEFLIN. I just wondered if there were any statistics that would show, from a study maybe conducted by the administrative office of the courts or someone, how long trustees usually take to determine whether they will accept or reject a lease or allow the landlord to proceed to try to obtain a lease.

Have there been any studies made? The administrative office of the courts makes all sorts of studies, and we see a lot of statistics and sometimes we get lost in the maze of statistics. But is anyone familiar with the fact that there has been a study to show that across the United States, there has been a delay?

Mr. WOODBURY. I do not have any statistics. My own observation is that it is a regional problem. It depends upon the personality of the particular court and trustee. In some cases, there is exceptional cooperation to try to minimize the length of time.

We were hoping that this law would more or less put some constraints or dictate a little more of a firm standard to the court and to the trustees to try to expedite matters. But, unfortunately, I do not have any statistics; I do not have any.

Senator HEFLIN. Mr. Holmes has outlined a narrative or a scenario of what has occurred to his shopping center in very graphic terms to illustrate the problem, with figures on individual retail outlets, which tells a mom-and-pop type of operation story. It is the ill effect of where a major tenant goes into bankruptcy and its effect upon the other tenants in that shopping center.

Are there other steps that the landlord and fellow tenants can take to curtail the adverse ripple effect after a major tenant goes into bankruptcy?

Mr. WOODBURY. I think the only steps I know of are before the major tenant goes into bankruptcy. The staying of actions puts you totally at the mercy of the trustee and the court. When I know a tenant is in trouble, I go and negotiate and do anything I can to try to get him out of possession before he files, because the court is not likely to come back in and try to take a property back under a preference arrangement, or something, where they have already abandoned possession.

Frankly, knowing the types of delays that are inherent in the act, our method usually is to do anything we can to get the tenant out of there before the filing. Once it is filed, I do not know of anything.

Senator HEFLIN. His example is where you have one retail grocery outlet and it has its effect. Some shopping centers go under the theory that you ought to have, at distant ends of a shopping center, two grocery retail outlets. If you lost one, you would not lose them both, or else there is some competition that enters into this.

I do not know enough about shopping center planning and that type of thing, but is there an effort being made to minimize the ripple effect of a major tenant going into bankruptcy?

I can see that if you make a mistake and get a wrong tenant and that is the only one in there, the other tenants are going to suffer, regardless of if you get a new one in there. People are just prone to buy from a name retail grocery outlet rather than just a replacement. If your Food Fair had a reputation and was doing a good job in retail, you have got it replaced in 4 or 5 months, but the ripple effect can go on for a good while.

Bankruptcy changes may minimize that, but I just wondered whether or not, in basic shopping center planning, that is a foreseeable problem and what steps ought to be taken to minimize the ill effects.

Mr. Oliver, you ought to have some ideas about this.

Mr. OLIVER. Senator, certainly I am sure the lawyers when they draw all the agreements contemplate that, and the developer does too. But whenever a major store closes, it is going to create a tremendous problem; if not for the entire center, it will create a real problem for the people who are close by to it.

In other words, in a mall you might have department stores on two ends. Well, if one closes, the tenants at that end of the mall will be the ones who suffer more greatly than the others. You can contractually provide anything, but once they are in bankruptcy, you are right back in court again.

We wrote some great agreements on bankruptcy back in the good old days, but they do not do us any good anymore. So, we are right back in court.

Senator HEFLIN. You are addressing basically straight bankruptcy. Now, under reorganization and other plans, are there peculiarities of problems that have adverse ripple effects upon the landlord and the cotenants?

Mr. OLIVER. Yes, sir. It is my limited experience, but even when they continue in business under a plan, and so forth, it is usually a pretty sad effect. A good example, while we do not own one of the stores, is Maison Blanche in New Orleans. You could walk in that store, and they were city stores. I believe they went into chapter 11 and then closed. But, you know, the merchandise starts going on. Their draw and their attraction as an anchor store diminishes greatly once they get in bankruptcy.

The Food Fair was not bankrupt; it just started out, and 1 day it did not have vegetables and the next week it did not have meat, and so forth. They go downhill. I am sure there are a lot of different considerations, but from a practical standpoint, it is still a substantial problem.

Mr. WOODBURY. I might also note that, getting out of a neighborhood center, if you lease your store spaces to try to create a high-end center because you feel that is what the market area justifies, you lease to different stores than you do if you are creating a lower end center.

Fashion Square in Van Nuys, Calif., has 5 stores that sell sterling silver and this type of thing, and I have 1 in a 175-store center in Utah. If you replaced I. Magnin or a quality department store with a Woolco—in lots of centers, I would rather have Woolco, but it would have a dramatic effect on the ability of the smaller tenants in that center that are catering to an entirely different market to succeed in the future.

Senator HEFLIN. What is the trend now in the United States? Are we going to move toward more and more shopping centers? Is this a growing business? Are you at a plateau where you are not growing, or what is the overall, basic future of the shopping center? Are any of you fixing to get into another business or are you going to stick with it?

Mr. WOODBURY. Well, I think that the shopping center provides a community need. It takes less gasoline mileage to get there; you can do your shopping in one stop. The trend in statistics is that a greater portion of the retailing is being done in shopping centers.

Now, shopping centers, like everyone else, are suffering from the problem of high interest rates, which are making aggressive development difficult. So, they are suffering like the rest of the economy. But, relatively speaking, I think there is a trend toward more shopping centers, although a very large number of them are being built in the central urban core instead of being rural and outlying today.

Senator HEFLIN. Thank you, gentlemen. We appreciate your testimony and your responses to questions and comments throughout. The committee will give careful consideration to your written and oral words alike. Thank you.

Mr. LAMBROSE. Thank you.

Mr. WOODBURY. Thank you, Mr. Chairman.

[The prepared statements and other submissions of Messrs. Woodbury, Oliver, Lambrose, and Holmes follow:]

PREPARED STATEMENT OF WALLACE R. WOODBURY

SUMMARY OF STATEMENT

As Congress recognized in enacting the Bankruptcy Reform Act of 1978 (the Bankruptcy Code or the Code), shopping center leases are unique among all leases of real property in that each lease arrangement involves not only the interests of that tenant and the landlord, but the interests of every other tenant of the shopping center. A shopping center is a combination of retailers each dependent on the others to attract shoppers to a specially designed structure intended to facilitate and encourage shopping. Thus, there is an interrelationship among the tenants of a shopping center such that the bankruptcy of one tenant has a serious impact on the other tenants.

Prior to the enactment of the Code, in the case of the bankruptcy of a tenant, the interests of the shopping center and its other tenants were protected by the contractual power of the lessor to control the disposition of the lease. Under the Code, clauses permitting the lessor to terminate the lease are unenforceable. However, because Congress recognized the special problems of shopping centers, special provisions regarding unexpired shopping center leases were included in the Code. These provisions, sections 365(b)(1)(C) and (b)(3), specify various assurances which the trustee is required to make in order to assume or assign an unexpired lease of the debtor.

Experience with these provisions indicates that they have not been functioning as originally intended by Congress. Several substantive and technical problems have arisen as follows:

A. Substantive Problems

1. The Code gives the trustee an option to assume or reject an unexpired lease. No time limit is established in the Code (except for liquidation cases), and an extended period of time can pass with the shopping center owner not knowing the disposition of the lease. If the space is not used as a retail store, the entire center can suffer irreparable injury because of decreased traffic, especially in the case of a major (anchor) tenant.

We propose that a 60-day time limit be placed on the trustee, permitting the court to allow additional time for cause.

2. During the time the trustee is deciding whether to assume or reject a lease, the landlord frequently does not receive rent and other payments required under the lease. Since the landlord has been deprived of his contractual right to terminate the lease upon bankruptcy, it would seem fair to require the trustee to perform all the obligations under the lease, including the payment of rent and other charges specified in the lease until the lease is assumed or rejected.

This provision would alter current law which permits a trustee to pay a warehouse value for space no longer being used for retail sales. These kinds of payments are particularly onerous to a shopping center landlord who has usually obtained financing based on receiving rent from retail use.

3. The Code requires "substantial" compliance with the lease provisions of critical importance to shopping centers. This introduces an ambiguity into the law as to how great a

deviation should be allowed. ICSC proposes that this ambiguity be removed and full compliance with these clauses be required.

4. If the trustee assigns the lease to a new tenant, the landlord is being placed in the highly unusual position of being forced into an interrelated business, similar to a joint venture, with a person he has not selected. We believe the law should require that the new tenant have a financial status equal to what the debtor-tenant had when the lease was first executed. This would assure that the new tenant meets the landlord's general financial requirements.

5. If the trustee assigns the lease to a new tenant, the law should specify that the landlord is entitled to his customary security deposit from the new tenant.

B. Technical Amendments

1. A problem has arisen that some trustees do not believe that an assignee of a shopping center lease has to comply with the use and other clauses contained in the lease being assumed. The Code should clarify that the new tenant must comply with all the provisions of the lease being assumed as well as assuring that there is no breach in other documents relating to the shopping center.

2. The critical provisions of the Code applicable to shopping centers only apply if there has been a default in the lease. These provisions should apply to any assignment of the lease whether or not there has been a default.

3. If a lease has terminated under state law prior to bankruptcy by reason of its own terms or a judicial order, that lease is no longer property of the debtor and should not be subject to the bankruptcy proceedings. We believe the law should clarify this point.

4. It is possible that a lease may terminate by its own terms while the bankruptcy proceedings are still pending, e.g., the term of the lease comes to an end. The Code should make it clear that the landlord can recover possession of the premises in such a situation.

I. Introduction

My name is Wallace R. Woodbury. I am an attorney and Chairman of the Board of Woodbury Corporation. The Woodbury Corporation is a 60 year old real estate development, brokerage, and management firm headquartered in Salt Lake City, Utah. It has been intimately involved in the development and management of regional, community, and neighborhood shopping centers as well as free-standing commercial, industrial, and office buildings. I am also a member of the Government Affairs Committee of the International Council of Shopping Centers (ICSC). I am testifying on behalf of my firm and the ICSC.

Contrary to the obvious Congressional intent, the 1978 Bankruptcy Reform Act unnecessarily and unreasonably impairs the right of a landlord to adequate remedies in the event of a tenant bankruptcy. In addition, the landlord and non-bankrupt tenants are often damaged by the arbitrary and capricious administration of the bankrupt estate by the bankruptcy trustee or court.

I am testifying in support of S. 2297, which would

eliminate certain inequities in the current Bankruptcy Code and provide more predictable administrative remedies.

A shopping center is a combination of retailers each dependent upon the others to attract shoppers to an especially designed structure intended to facilitate and encourage shopping. As a result of such a relationship, the bankruptcy of one tenant often has a serious impact on the other tenants. A successful shopping center is typically the result of sophisticated planning and a delicate balance of merchants. Tenants are chosen on the basis of their business image and use, an analysis and evaluation of the market demands of the area and an examination of the financial capacity and business experience of tenant in relation to the potential customers to be served. A well-planned project with a balanced mix of stores maximizes the potential benefits to the landlord, the tenants, and the community served.

Shopping center leases are necessarily made on a long-term basis considering the large investment usually made by tenants in preparing their establishments for the contemplated business. These long-term lease arrangements, which are granted to tenants for specific and limited uses of the landlord's property for long periods of time, put the landlord into a position unlike that of a merchandise creditor or financial institutional lender. Such suppliers or lenders can make periodic short-term reviews of the financial condition of their customers and can freely terminate credit when they feel the customers capacity to pay is impaired. A landlord under a long-term agreement cannot do so.

Shopping center leases usually contain strict limitations on use, affirmative covenants relating to radius clauses (forbiding the dilution of tenants market potential), prohibitions on assignments unless the landlord is satisfied with the financial stability, credit, public image, and intended use of the potential assignee, and specific requirements for cooperative advertising, promotion, common area use and maintenance, sign control, and uniform hours of operation.

The vacancy of any tenant space for an extended period of time can seriously disrupt not only the neighboring tenants but an entire shopping center. Customer traffic is reduced not only by the decreased supply of products or services, but also by the less pleasant atmosphere resulting from "boarding up" a portion of the shopping center. Where the vacant space is that of an anchor store, the effect on the shopping center and its other tenants can be devastating.

The assignment of a lease to a tenant in the same business as other existing tenants might substantially reduce the revenues of these tenants, thereby jeopardizing their solvency and affecting their ability to pay their rent. In addition, the amount of the guaranteed minimum rent and the percentage rental rates paid by shopping center tenants in most instances is dependent upon type of business of that particular tenant and some businesses traditionally pay higher square foot rentals and have higher percentage rentals than tenants operating other businesses. The assignment of a lease to a tenant in a business other than that of the assignor could give the assignee an unfiar advantage over existing tenants in the same business who are paying the higher rental rates consistent with the nature of their business.

Prior to enactment of the Bankruptcy Reform Act of 1978 (the Code), the shopping center owner could protect the rights and interests of the other tenants in the shopping center by

enforcing contractual lease provisions permitting the termination or restricting the assignment or other disposition of the lease in the case of a bankruptcy. Under the Code such provisions became unenforceable, and the fate of the lease came under the control of the trustee of a bankrupt tenant.

Such trustees are granted considerable discretion under the Code, particularly in Chapter XI proceedings. However, Congress recognized the special problems of shopping centers by enacting special provisions in Sections 365(b)(1)(C) and (b)(3), specifying criteria which the trustee is required to meet in order to affirm or assign an unexpired lease of the debtor.

Unfortunately, however, in actual practice the specification of such criteria has not proved adequate to provide the kind of protection which Congress intended. For instance, one of the most oppressive problems faced by shopping centers results from the failure of the Code to require the trustee to accept or reject the unexpired lease within a specified time limit in a nonliquidation bankruptcy proceeding.

Also, there is no time limit specified requiring the trustee to release jurisdiction over an unwanted leasehold or even an expired lease to allow the landlord to institute proceedings to recover possession, even though the former tenant has filed to vacate the premises, or the lease has expired and the tenant is holding possession by sufferance only.

Some trustees refuse to recommend release of the premises even where they know full well that there is no interest of the tenant to be preserved for the bankruptcy estate. In the meantime, the landlord may not re-rent the premises or prosecute any action to recover possession because all state court proceedings are "stayed." Other non-bankrupt tenants are usually damaged by the vacancy. On some occasions, even where the trustee has recommended that the property be released to the landlord because there is no value to be preserved for the bankruptcy estate, the court rejects the recommendation or merely avoids making any decision.

For example, in two cases where Hermes Associates, operating two shopping centers known as the Family Center in Las Vegas, Nevada, had leased to a California based tenant known as "Brandalls," the tenant filed for bankruptcy under Chapter XI on March 16, 1981. Rents were paid through 1980. The trustee recommended to the court that the vacant leasehold interest resulting from the bankrupt moving from the premises be surrendered to the landlord. Nonetheless, the California court refused to take any action and in order to obtain permission to pursue an action to recover the premises the landlord was required to pay $2,000 to the bankrupt estate. After such payment, possession was surrendered to the landlord in July, and the new tenants were ultimately located in October. The landlord received no rental for the period from January through September.

In another case, in Ogden, Utah we had leased a space to Odyssey Records and Tapes, a California headquartered company, and the adjacent space was occupied by a complimentary tenant, Stokes Brothers, a TV, electronics, and computer business. Odyssey exercised a renewal option, and, almost immediately thereafter, filed a bankruptcy petition and vacated the premises. The lease limited the use of the property to retail sale of records and tapes, and forbade any assignment without the consent of the landlord. The trustee refused to pay rent or release the premises to the landlord despite the fact that the landlord had a substitute replacement tenant with substantial assets who

complied with the use restriction available to rent the property. Over the landlord's objection, the trustee in the California court sold and assigned the lease to a shell corporation named Rocky Mountain Sales which sold substantially the same types of merchandise as the neighbor tenant, Stokes Brothers, and which advertised "going out of business prices." The landlord objected without avail to the changed use of the space, the inadequate capital of the new tenant and the use of prohibited promotional advertising methods by the new tenant. After 6 months of ruinous competition, the Stokes Brothers abandoned the premises on the grounds that the landlord had given them an exclusive commitment and this commitment had been violated. After 13 months, the trustee's tenant, Rocky Mountain, abandoned the premises, and left substantial amounts of delinquent rent and physical damage to the premises. However, the landlord was without remedy because Rocky Mountain was impecunious. Thus, the landlord ended up with vacancies in two stores, the substantial loss of rental income, and considerable building damage and the nonbankrupt tenant lost substantial sums and was forced to abandon the shopping center because of the trustee's utter disregard of the lease provisions which were designed to protect both the landlord and the non-bankrupt adjacent tenant.

In another Utah shopping center case in 1981, relating to a building at 3600 South and 600 West Salt Lake Valley, Morris T. Anderson tried to prosecute default proceedings against its tenant Alpha Corporation which had filed Chapter XI. The law requires a plan to be submitted within 120 days. However, no plan has been submitted after more than eight months. Despite this, the court has been unwilling to release the property to the landlord, and there has been to date a rental loss of more than $35,000. In addition, although the lease granted the landlord a lien on the tenant's furnishings and equipment, the Court is conducting an auction to sell the tenant's equipment this week and has not given the landlord permission to prosecute any action to protect its interest.

Another current bankruptcy case involves a nine thousand square foot Hughes and Hatcher store in the Severn Mall Shopping Center in Cleveland. The tenant is headquartered in New York and the lease expires January 31, 1983. The tenant closed its doors in the Cleveland Shopping Center, and moved out on February 1, 1982. Subsequently the tenant filed Chapter XI proceedings in upstate New York. Despite the fact that the trustee and the attorneys for the bankrupt have both stated that such a short leasehold has no value and should be surrendered to the landlord, the New York court has refused to make any decision to accept or reject the lease because no formal reorganization plan has yet been filed.

These are examples of the types of situations that would be cured by the language of S. 2297. These provisions would provide reasonable protection to the landlord and the non-bankrupt tenants of a shopping center from the extended delays and losses resulting from the bankruptcies of other tenants in the shopping center.

We respectfully urge the adoption of this bill.

II. The Unique Nature of Shopping Center Leases

The International Council of Shopping Centers (ICSC) is a business association of more than 10,000 members. About 63% of our members develop and/or own shopping centers. About 15% are retail companies, the major share of whose stores are operated in shopping centers. Most of our developer-owner members own from

two to four shopping centers each, and collectively represent a major share of the estimated 22,700 shopping centers in the United States in 1982.

After World War II, the changes in the patterns of American life produced by the advent of the automobile were accelerated, and nowhere were these changes more evident than in the retail industry. Previously, retail trade was concentrated in individual stores in central business districts, but by 1981, 42.0% of all U.S. retail trade amounting to $438.8 billion was conducted in shopping centers. It is estimated that in the 1982-83 period 60% of total new retail square footage constructed will be in shopping centers. In the same period about 88% of new department store square footage will be constructed in shopping centers.

What makes this type of operation possible is the understanding by all concerned that the commercial success of the enterprise depends on the finished product functioning as a unit, presenting to the public a single face.

What makes this type of operation desirable is the fact that experience has shown that a combination of tenants ("tenant mix") that is well designed to serve the "trade area" of a shopping center will have a symbiotic effect on business in the center that will benefit all of the tenants. It is for this reason that businesses are willing to pay a premium to directly compete with each other in close proximity in a shopping center.

The joint effort of a shopping center is cemented by a series of master agreements, entered into by all the parties involved in a shopping center, that set forth in precise terms the rights and obligations of each party.

When a center includes major department stores, it is common (but not universal) practice for the department stores to own their own buildings and, also, usually (but again, not always) some part of the land within the center's perimeter.

With the department stores each owning a share of the site and the developer owning the portion occupied by the satellite stores, and with the structures all physically tied together, a shopping center can become a complicated endeavor. To further complicate matters, each party finances its investment with a separate mortgage. The result is a real estate development in which numerous entities hold long-term, effectively inseparable interests.

The standard pattern has always been for the tenants to pay rent on the basis of a percentage of their sales volume or a guaranteed minimum amount, whichever is greater. Exceptions to the pattern have become progressively fewer; today they are rare and are confined to special situations.

As shopping centers have developed, they have become larger and more sophisticated in design, construction and concept, and they involve tens of millions of dollars of investments by the developer, the tenants, and financial institutions.

In addition, because of their size and impact on development patterns, the construction of a shopping center often involves the expenditure of millions of dollars of public money on infra-structure such as roads, traffic control, and water and sewage facilities. Of course, these expenditures are returned to the governments involved through taxes on the business activity generated by the shopping center.

Thus, a shopping center, if successful, is the product of considerable sophisticated planning and consists of a delicate balance of merchants. Tenants are chosen on the basis of their business use, their type of operation, the market they will cater to (age grouping, financial status, etc.), financial viability, and business experience. The choosing of types of tenants takes into consideration the needs of the surrounding community and the appeal of the stores, as a whole, to a broad segment of the population. A well planned project will have a percentage of ready-to-wear merchants, shoe stores, food establishments, gift shops, book stores, service establishments, etc. A center so planned is protective of the tenants, and the landlord, and satisfies as well the needs of the community to which it usually contributes considerable tax dollars.

This is true not only for large shopping centers, but also for small centers where independent merchants depend upon one another to attract customers from whom they mutually benefit.

Shopping center leases are necessarily made on a long-term basis considering the large investment usually made by tenants in preparing their establishments for the contemplated business. These long-term lease agreements granting to tenants the use of the landlord's property for such long periods of time puts the landlord into a position unlike a merchandise creditor or a financial institutional lender. Such suppliers or lenders can make periodic reviews of the financial condition of their customer and can, freely, stop credit or loans at such time as they, in their discretion, feel that the credit of their customer is impaired. A landlord, under a long-term agreement, cannot do so.

Moreover, shopping center leases frequently contain "anchor" clauses which commit a given tenant to a lease term only so long as another designated tenant remains a tenant in the shopping center. These provisions further manifest the symbiotic, interdependent nature of a shopping center.

III. The Consequences to Shopping Centers and Their Tenants of Vacant or Partially Operated Space or Space Used for Purposes Other Than Specified in Lease Agreements

As discussed above, the success of a shopping center, and thus of all of its tenants, is based in large part on its "tenant mix." To operate properly, the tenant space in the shopping center must be fully occupied by establishments operating at full capacity and offering products or services which, in conjunction with those offered by other tenants, are designed to maximize the attraction of customers to the shopping center.

The vacancy of any tenant space for an extended period of time can seriously disrupt an entire shopping center. Customer traffic is reduced not only by the decreased supply of products or services, but also by the less pleasant atmosphere caused by boarding up a portion of the shopping center. Where the vacant space is that of an anchor store, the effect on the shopping center and its other tenants can be devastating. Indeed, even a curtailment of the operation of an anchor tenant can substantially reduce the traffic of an entire shopping center.

Another consequence of the curtailment of operation of any tenant is a reduction of rental revenues to the shopping center. This occurs because almost all shopping center tenants pay rent which is, at least in part, based on a percentage of

their sales volume. Typically, this percentage rental is at least as important to the shopping center as is the minimum base rental.

The operation of a shopping center can also be seriously impaired by the use of any tenant space for purposes other than those contemplated by the shopping center and its other tenants and provided for in a master lease or other agreement. For example, the assignment of a lease to a tenant in the same business as other existing tenants could substantially reduce their revenues, thus affecting their ability to pay their rent and jeopardizing their solvency. Moreover, interim or long-term loan agreements sometimes contain covenants restricting the type or quality of tenant which would be accepted in the shopping center. If the use provisions of a lease agreement are not complied with, the lessor could be in violation of such loan covenants, thereby causing acceleration of the indebtedness to the lessor's lender.

In addition, the amount of rent paid by shopping center tenants is in most instances based upon the business of that tenant's space. Tenants operating certain businesses pay a much higher square foot rental than tenants operating other businesses. The assignment of a lease to a tenant in a business other than that of the assignor could give the assignee an unfair advantage over existing tenants who are paying a higher square footage rent based upon the nature of their business.

IV. The Law Regarding Unexpired Shopping Center Leases Held by Bankrupt Tenants

A. The Law Prior to the Bankruptcy Reform Act of 1978

Prior to the enactment of the Code, in the case of the bankruptcy of a tenant, a shopping center was able to protect its interest and the interests of its other tenants by enforcing lease clauses permitting the lessor to control the lease. Shopping center leases thus generally provided that if insolvency proceedings were filed, the lessor could: 1) terminate the lease; 2) change the lease to a month-to-month tenancy; 3) waive or terminate an option to renew the lease; or 4) terminate the lease if the debtor was unable to maintain a certain sales volume or net worth.

Such provisions enabled the shopping center to avoid the adverse consequences of vacancies, curtailed operations or inappropriate uses described above in the event that any tenant became insolvent.

B. Section 365 of the Bankruptcy Code: Language, Structure and Legislative History

Section 365 of the Bankruptcy Code relates to executory contracts and unexpired leases. Subsections (a), (b)(1), (b)(3), (d)(1), (d)(2), (e)(1), (f)(1) and (f)(2) are of primary importance regarding unexpired shopping center leases. These sections provide as follows:

> (a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.
>
> (b)(1) If there has been a default in an executory contract or unexpired lease of the debtor,

the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

(C) provides adequate assurance of future performance under such contract or lease.

* * *

(b)(3) For the purposes of paragraph (1) of this section, adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance--

(A) of the source of rent and other consideration due under such lease;

(B) that any percentage rent due under such lease will not decline substantially;

(C) that assumption or assignment of such lease will not breach substantially any provision, such as a radius, location, use, or exclusivity provision, in any other lease, financing agreement, or master agreement relating to such shopping center; and

(D) that assumption or assignment of such lease will not disrupt substantially any tenant mix or balance in such shopping center.

* * *

(d)(1) In a case under chapter 7 of this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected.

(d)(2) In a case under chapter 9, 11, or 13 of this title, the trustee may assume or reject an executory contract or unexpired lease of the debtor at any time before the confirmation of a plan, but the court, on request of any party to such contract or lease, may order the trustee to determine within a specified period of time whether to assume or reject such contract or lease.

(e)(1) Notwithstanding a provision in an executory contract or unexpired lease, or in applicable law, an executory contract or unexpired lease of the debtor may not be terminated or modified, and any right or obligation under such contract or lease may not be terminated or modified, at any time after the commencement of the case solely because of a provision in such contract or lease that is conditioned on--

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

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(B) the commencement of a case under this title; or

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

* * *

(f)(1) Except as provided in subsection (c) of this section, notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law, that prohibits, restricts, or conditions the assignment of such contract or lease, the trustee may assign such contract or lease under paragraph (2) of this subsection.

(f)(2) The trustee may assign an executory contract or unexpired lease of the debtor only if--

(A) the trustee assumes such contract or lease in accordance with the provisions of this section; and

(B) adequate assurance of future performance by the assignee of such contract or lease is provided, whether or not there has been a default in such contract or lease.

Subsection (e)(1) makes the formerly employed termination clauses unenforceable. Subsections (b)(1) and (f) permit the trustee to assume or assign an unexpired lease subject to other provisions of this section. Subsection (b)(1)(C) and (f)(2)(B) require adequate assurances of future performance in the case of the assumption or assignment, respectively, of an unexpired lease. Subsection (b)(3) makes explicit what specific assurances of future performance are required in the case of a shopping center lease.

By these provisions, the right of a trustee to assume an unexpired shopping center lease under which there is an existing default is limited not only by the general provisions of subsection (b)(1), but also by the specific "shopping center" provisions of subsection (b)(3). The purpose of these provisions is to ensure that an unexpired shopping center lease is assumed by the trustee only where the trustee provides adequate assurance that there will be performance by the trustee under the debtor's lease in the future, and that that performance will include assurances of the source of rent, that the percentage rent due would not decline substantially (because of reduced sales), that the use provisions contained in any other lease, financing agreement or master agreement would not be substantially breached, and that the tenant mix would not be substantially disrupted.

That Congress intended to provide special protections for shopping centers and their solvent tenants regarding the assumption by a trustee of an unexpired lease is thus demonstrated not only by the language of these provisions, but also by their structure. Because of the concern about the ripple effect of a tenant bankruptcy, the shopping center industry is the only industry which Congress determined to protect with a specific provision, Section 365(b)(3).

An examination of the legislative history of these provisions explains and provides further support for the proposition that Congress intended to effectively prevent shopping

centers and their solvent tenants from being unnecessarily injured in the event that one tenant became insolvent.

As introduced, section 365(b)(1) and (f)(2) of H.R. 8200 required that "adequate assurances" of future performance be provided the lessor in the case of either an assumption or assignment by a trustee of an unexpired lease. The shopping center industry argued that this requirement was too vague to effectively solve the problems which would be encountered by shopping centers in the event of the assumption or assignment of a lease.

The House Judiciary Committee responded to these arguments by including in its report the following language:

> The unenforceability of ipso facto or bankruptcy clauses proposed under this section will require the courts to be sensitive to the rights of the nondebtor party to executory contracts and unexpired leases. If the trustee is to assume a contract or lease, the courts will have to insure that the trustee's performance under the contract or lease gives the other contracting party the full benefit of his bargain. An example of the complexity that may arise in these situations and the need for a determination of all aspects of a particular executory contract or unexpired lease is the shopping center lease under which the debtor is a tenant in a shopping center.
>
> A shopping center is often a carefully planned enterprise, and though it consists of numerous individual tenants, the center is planned as a single unit, often subject to a master lease or financing agreement. Under these agreements, the tenant mix in a shopping center may be as important to the lessor as the actual promised rental payments, because certain mixes will attract higher patronage of the stores in the center, and thus a higher rental for the landlord from those stores that are subject to a percentage of gross receipts rental agreement. Thus, in order to assure a landlord of his bargained for exchange, the court would have to consider such factors as the nature of the business to be conducted by the trustee or his assignee, whether that business complies with the requirements of any master agreement, whether the kind of business proposed will generate gross sales in an amount such that the percentage rent specified in the lease is substantially the same as what would have been provided by the debtor, and whether the business proposed to be conducted would result in a breach of other clauses in master agreements relating, for example, to tenant mix and location.

H.R. Rep. No. 595, 95th Cong., 1st Sess., 348-349 (1977).

The Senate Judiciary Committee responded to these concerns by incorporating in S. 2266 the following language:

* * *

> (b)(3) The provisions of paragraph (1) of this subsection shall not prevent termination of a lease pursuant to provisions contained therein--
>
> (A) in a case under chapter 7 of this title;

> (B) where the lease was entered into before the effective date of this title;
> (C) where the property leased thereunder is not essential to the debtor's business;
> (D) where the rent payable pursuant to the lease is substantially less than the fair rental value of the property leased thereunder; or
> (E) where the lease contains provisions for rent contingent upon the lessee's profits or sales and the rent otherwise set forth in the lease was substantially less than the fair rental value of the property at the time the lease was entered into.
>
> * * *
>
> (b)(5) For purposes of this subsection, "adequate assurance" shall include with regard to an unexpired lease of the debtor reasonable assurance--
>
> (A) of the source of rental payments and other consideration due and owing to the landlord under the lease agreement;
> (B) that there will be no substantial decline in any percentage rates specified by the lease;
> (C) that the assignment or assumption of the lease will not substantially breach clauses (including, but not limited to, radius, location, use, and exclusive clauses) in other leases, financing agreements, or a master agreement relating to the leased and adjoining leased premises; and
> (D) that an assumption or assignment of a lease will not disrupt the tenant mix or balance in property subject to multiple individual leases and an overall master agreement.

Further, the Senate Committee made clear in its report that subsection (b)(5) was intended to assist shopping centers.

> Subsection (b)(5) provides that in lease situations common to shopping centers, protections must be provided for the lessor if the trustee assumes the lease, including protection against decline in percentage rents, breach of agreements with other tenants, and preservation of the tenant mix. Protection for tenant mix will not be required in the office building situation.

S. Rep. No. 989, 95th Cong., 2nd Sess., 59 (1978).

By agreement of the Senate and House floor managers of this legislation, a compromise bill was introduced which contained the language in subsection (b)(3) which was ultimately enacted.

In the Senate and House debates on the compromise bill, this provision was described as follows:

> Section 365(b)(3) represents a compromise between H.R. 8200 as passed by the House and the Senate amendment. The provision adopts standards contained in section 365(b)(5) of the Senate amendment to define adequate assurance of future performance of a lease of real property in a shopping center.

124 Cong. Rec. S17409 (daily ed., Oct. 6, 1978) (remarks of Sen. De Concini); 124 Cong. Rec. H11093 (daily ed, Sept. 28, 1978) (remarks of Mr. Edwards).

V. Problems Under the Code and Proposed Solutions

A. Substantive Amendments

1. Time Limit on Acceptance or Rejection of Lease

The 1978 Act presented landlords with a new problem by voiding lease clauses that terminated the tenancy on bankruptcy and by providing, in §365 of the Code, that the trustee may assume or reject the unexpired lease of the debtor. No time limit is imposed on this action. This has created serious problems for shopping centers when space has been either left vacant for an extended period of time without providing the landlord an opportunity to relet the premises to a new tenant or a store has operated at a minimum level.

Under the current law, the trustee can keep the landlord in this ambiguous position for several months. Frequently, the landlord is forced to make a payment to the trustee to extricate himself from this difficulty. As indicated above, other retailers in the center, as well as the landlord, suffer uncompensated losses during this period. Accordingly, the payment is not based on the value of the lease but is in the nature of ransom to save the rest of the center.

This problem is especially acute when the debtor was the anchor tenant which was intended to attract customers to the center and on which the other retailers relied for traffic. It is fundamental that a shopping center cannot function properly without a viable anchor tenant. In the event of its bankruptcy, it must either be revitalized promptly or replaced. An extended vacancy will destroy the center. Although the landlord has the right to file a motion to require the trustee to assume or reject the lease, this procedure requires so much time for completion that it frequently exacerbates the problem.

ICSC proposes that §365(d) of the Code be amended to read as follows:

> (d) In all cases under this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected, and in the case of a lease, the court shall order the premises to be vacated immediately. If the premises are not vacated within 30 days after such order, the trustee shall perform all of the obligations under such lease currently. Acceptance of such performance shall not constitute a waiver or relinquishment of the lessor's rights under the lease or the Bankruptcy Code.

2. Payment of Current Rent and Performance of Lease Obligations

Although rent during the period of administration of the estate is treated as an administrative expense, that does not constitute sufficient protection under the new law which permits the trustee to remain in possession of the premises for an extended period of time. This presents a hardship to a landlord who may not receive rent for several months and is unable to gain

control of his premises. We are not aware of any other class of person who is required to provide a service to the bankrupt estate without current compensation.

Cases have permitted trustees to pay a warehouse value rent for space no longer being used for retail sales. This is grossly unfair to a landlord who has developed a shopping center for retail business and has obtained financing based on the stream of rents from retail rental use.

Similar considerations apply to the other obligations under the lease. Until the lease is rejected, the trustee should perform all obligations under the lease to prevent serious damage to the shopping center and the other tenants:

ICSC proposes to add the following sentence to §365(a):

> The trustee shall timely perform all the obligations of the tenant arising from and after the date of the order for relief, under an unexpired lease (including payment of the rent and other charges specified in such lease) until such lease is assumed or rejected, notwithstanding the provisions of §503.

3. Deletion of "substantially" Standard

The section inserted in the Code for the protection of shopping centers is §365(b)(3). While inclusion of the word "substantially" in subsection (B) of this section (requiring payment of percentage rent) may be appropriate because the law cannot guarantee a particular level of rent, the word "substantially" is not appropriate for subsections (C) and (D) (regarding the breach of other agreements and the disruption of the tenant mix). These are the critical provisions which are intended to assure that the business of the shopping center is preserved and the other tenants are not unduly injured by the bankruptcy proceedings. This requires that the specified clauses are not breached and that the tenant mix will not be disrupted by the action of the trustee. The use of the word "substantially" in these subsections inserts a major ambiguity into these critical provisions regarding how great a deviation will be allowed. This ambiguity has allowed some debtors to completely ignore the use clauses of their lease and advertise their space for "all retail uses." (See the Attachment for a current example.)

ICSC proposes that the word "substantially" be deleted from §365(b)(3)(C) and (D) to avoid these kinds of disputes.

4. Financial Status of New Tenant

Another problem presented by the Code's permitting the trustee to place a new tenant in a shopping center without the consent of the landlord is that the tenant, although solvent, may not be of the same financial quality as the landlord originally contracted for. This situation presents an exception to the fundamental principle of our law that businessmen are usually entitled to determine the persons with whom they wish to do business. If the trustee is going to assign the lease to a new tenant, that tenant should have the same financial standing as the original tenant had when the lease was signed.

ICSC proposes to solve this problem by adding the following language to Section 365(b)(3)(A):

> ...with a financial standing, including guarantors,

similar to that of the original tenant when the lease was executed;

5. Security Deposits From New Tenants

If a landlord is required to accept a new tenant, then he is entitled to a security deposit in the same manner as is required from other tenants, and as utilities are allowed deposits under §366 of the Code.

ICSC proposes that a new subsection (l) be added to §365 to read as follows:

> (l) If an unexpired lease is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.

B. Technical Amendments

1. Assumption of Provisions of the Lease

Section 365(b)(3)(C) of the Code provides that a trustee, when assuming a lease of property in a shopping center, must provide adequate assurance that the assumption will not breach substantially specified provisions "in any other lease, financing agreement, or master agreement relating to such shopping center...." In at least two instances, trustees have taken the position that the requirement to comply with use clauses of all other leases implies that they do not have to comply with the use clause of the lease they are assuming. This would seem to be an erroneous interpretation of the law because §365(b)(1)(C) requires providing adequate assurance of future performance under the lease, and that ordinarily includes all of the terms and provisions of the lease.

In view of the difficulties which have been encountered, ICSC proposes that §365(b)(3)(C) of the Code be amended to read as follows:

> (C) that such assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited) to provisions, such as a radius, location, use, or exclusivity provision, and would not breach any such provision contained in any other lease, financing agreement, or master agreement relating to such shopping center; and

2. Requirements for Assumption of Lease Regardless of Default

A technical problem exists in that Section 365(b)(3), the provision intended to protect shopping centers, applies only for "purposes of paragraph (1)," and that paragraph only applies "If there has been a default in an executory contract or unexpired lease of the debtor...". There is no justification for this limitation and the provisions of Section 365(b)(3) should apply to any assumption or assignment of a shopping center lease whether or not there has been a default.

ICSC suggests that this problem can be solved by

amending the introductory language of Section 365(b)(3) to read as follows:

> (3) For purposes of paragraph (1) of this section and paragraph (2)(B) of section (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance -

3. Termination of Leases Prior to Bankruptcy

It is desirable to clarify the Code to establish that leases terminated under state law, by their own terms or judicial action, prior to bankruptcy are not subject to the bankruptcy proceedings. This would avoid problems of resurrection of terminated agreements.

ICSC proposes that a new Section 365(c)(3) be added to the Code to read as follows:

> (3) such contract or lease has been terminated under state law prior to the order for relief.

4. Termination of the Term of the Lease

It is possible that a lease will terminate by its own terms while the bankruptcy proceeding is still pending. It is possible to argue that the stay under §362 of the Code prevents a landlord from taking possession of the premises in accordance with a lease that has been terminated by expiration of the stated term.

ICSC proposes that a new subsection 9 be added to §362(b) as follows:

> "under subsection (a) of this section, of a proceeding to obtain possession of property subject to a lease which has expired by virtue of its own terms without regard to the bankruptcy proceedings.

Proposed Amendments

A. BRIEF DESCRIPTION

The proposed amendments to Section 365 would accomplish the following:

1. Impose a 60 day limit on a trustee's acceptance or rejection of an unexpired lease in all bankruptcy cases, with the right to request additional time for cause. If the premises are not vacated within 30 days after a court order, the trustee will be required to perform all of the obligations under the lease currently.

2. Require the trustee to perform all of the obligations of the tenant under the lease, including payment of rent and other charges specified in the lease, until the lease is assumed or rejected.

3. Delete the word "substantially" from the provisions requiring that an assignment of a shopping center lease would not breach other agreements and would not disrupt tenant mix.

4. Require the trustee to find that an assignee of a shopping center lease would have a financial standing similar to that of the original tenant.

5. Allow the lessor, in the event of a lease assignment, to require his customary security deposit from the new tenant.

6. Clarify that any assignment of a lease is subject to all of the provisions of the lease being assigned as well as assuring no breach in any other relevant document.

7. Provide that the special provisions for assignment of shopping center leases apply whether or not there has been a default under the lease.

8. Clarify that leases that have been terminated under state law will not be treated as property of the debtor subject to bankruptcy.

The proposed amendment to Section 362 would delete from the automatic stay provisions of that section, a proceeding to obtain possession of property subject to a lease which has expired by its own terms without regard to the bankruptcy proceedings.

B. Relevant Provisions, as Amended

§ 365. Executory contracts and unexpired leases

(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor. The trustee shall timely perform all the obligations of the tenant arising from and after the date of the order for relief, under an unexpired lease (including payment of the rent and other charges specified in such lease) until such lease is assumed or rejected, notwithstanding the provisions of §503.

(b)(1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

(C) provides adequate assurance of future performance under such contract or lease.

(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to--

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title; or

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

(3) For the purposes of paragraph (1) of this section and paragraph (2)(B) of section (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance--

(A) of the source of rent and other consideration due under such lease with a financial standing, including guarantors, similar to that of the original tenant when the lease was executed;

(B) that any percentage rent due under such lease will not decline substantially;

(C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach [substantially] any such provision[, such as a radius, location, use, or exclusivity provision,] contained in any other lease, financing agreement, or master agreement relating to such shopping center; and

(D) that assumption or assignment of such lease will not disrupt [substantially] any tenant mix or balance in such shopping center.

(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.

(c) The trustee may not assume or assign an executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--

(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

(B) such party does not consent to such assumption or assignment; or

(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor.

(3) such contract or lease has been terminated under state law prior to the order for relief.

(d)[(1) In a case under chapter 7 of this title,] In all cases under this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected, and in the case of a

lease, the court shall order the premises to be vacated immediately. If the premises are not vacated within 30 days after such order, the trustee shall perform all of the obligations under such lease currently. Acceptance of such performance shall not constitute a waiver or relinquishment of the lessor's rights under the lease or the Bankruptcy Code.

[(2) In a case under chapter 9, 11, or 13 of this title, the trustee may assume or reject an executory contract or unexpired lease of the debtor at any time before the confirmation of a plan, but the court, on request of any party to such contract or lease, may order the trustee to determine within a specified period of time whether to assume or reject such contract or lease.]

. . .

(1) If an unexpired lease is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.

§ 362. Automatic stay

(b) The filing of a petition under section 301, 302, or 303 of this title does not operate as a stay--

. . .

(9) under subsection (a) of this section, of a proceeding to obtain possession of property subject to a lease which has expired by virtue of its own terms without regard to the bankruptcy proceedings.

C. Side-by-Side Comparison of Present Law and Proposed Amendments

Present Law	Proposed Law
§ 365. Executory contracts and unexpired leases	§ 365. Executory contracts and unexpired leases
(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.	(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor. The trustee shall timely perform all the obligations of the tenant arising from and after the date of the order for relief, under an unexpired lease (including payment of the rent and other charges specified in such lease) until such lease is assumed or rejected, notwithstanding the provisions of §503.

Present Law

(b)(1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

(C) provides adequate assurance of future performance under such contract or lease.

(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to--

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title; or

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

(3) For the purposes of paragraph (1) of this section, adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance--

(A) of the source of rent and other consideration due under such lease;

Proposed Law

(b)(1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee--

(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

(C) provides adequate assurance of future performance under such contract or lease.

(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to--

(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

(B) the commencement of a case under this title; or

(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

(3) For the purposes of paragraph (1) of this section and paragraph (2)(B) of section (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance--

(A) of the source of rent and other consideration due under such lease with a financial standing, including guarantors, similar to that of the original tenant when the lease was executed;

Present Law	Proposed Law
(B) that any percentage rent due under such lease will not decline substantially;	(B) that any percentage rent due under such lease will not decline substantially;
(C) that assumption or assignment of such lease will not breach substantially any provision, such as a radius, location, use, or exclusivity provision, in any other lease, financing agreement, or master agreement relating to such shopping center; and	(C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other lease, financing agreement, or master agreement relating to such shopping center; and
(D) that assumption or assignment of such lease will not disrupt substantially any tenant mix or balance in such shopping center.	(D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center.
(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.	(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.
(c) The trustee may not assume or assign an executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--	(c) The trustee may not assume or assign an executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if--
(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and	(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

Present Law	Proposed Law
(B) such party does not consent to such assumption or assignment; or	(B) such party does not consent to such assumption or assignment; or
(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor.	(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor.
	(3) such contract or lease has been terminated under state law prior to the order for relief.
(d)(1) In a case under chapter 7 of this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected.	(d) In all cases under this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemend rejected, and in the case of a lease,, the court shall order the premises to be vacated immediately. If the premises are not vacated within 30 days after such order, the trustee shall perform all of the obligations under such lease currently. Acceptance of such performance shall not constitute a waiver or relinquishment of the lessor's rights under the lease or the Bankruptcy Code.
(2) In a case under chapter 9, 11, or 13 of this title, the trustee may assume or reject an executory contract or unexpired lease of the debtor at any time before the confirmation of a plan, but the court, on request of any party to such contract or lease, may order the trustee to determine within a specified period of time whether to assume or reject such contract or lease.	(1) If an unexpired lease is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.

THE WALL STREET JOURNAL
Friday, March 19, 1982

- Sample Lease Assignment Advertisement

REAL ESTATE FOR SALE REAL ESTATE FOR SALE REAL ESTATE FOR SALE

BANKRUPTCY SALE MARCH 25, 1982

PRIME SPACE AVAILABLE IN QUALITY MALLS

COUNTRY JUNCTION, COUNTRY LEGEND AND HOUSE OF JEANS

- VARIOUS LEASEHOLD TERMS OF 1-10 YEARS
- 1500-5000 SQ. FT. AVAILABLE
- ALL RETAIL USES CONSIDERED
- STORES PREVIOUSLY TRADED AS:

  ZIPPERS, COUNTRY LEGEND, PANTS SOUTH, HOUSE OF JEANS, DEPOT, JUNCTION, THE JUNCTION, WESTERN JUNCTION, JEANS AND TOPS, JUNIOR JUNCTION.

- STORES LOCATED IN ENCLOSED REGIONAL MALLS:

  MARYLAND (6); VIRGINIA (14); PENN. (4); ALA. (1); N.Y. (2); CONN. (1); N.J. (1); TENN. (1); ILLINOIS (2); GEORGIA (1); TEXAS (31); FLA. (3); OKLAHOMA (6); ARK. (4); MISS. (4); LA. (5); N.M. (1).

BANKRUPTCY SALE WILL BE HELD MARCH 25, 1982 AT 9:00 AM IN COURTROOM NO. 1 OF THE U.S. BANKRUPTCY COURT, 3rd FLOOR, U.S. POST OFFICE BUILDING, 615 E. HOUSTON STREET, SAN ANTONIO, TEXAS

FOR FURTHER INFORMATION CONTACT:
DAN S. GOLINSKY, V.P.

STONE-EAST ASSOCIATES, INC.
40 WEST 57 ST., NEW YORK, NY 10019 (212) 977-3100

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The Wall Street Journal, Friday, March 19, 1982

THE REAL ESTATE CORNER

HOW TO ANSWER BOX NUMBER ADS: All replies to WSJ box numbers that appear without an address should be sent to The Wall Street Journal, 22 Cortlandt St., New York, N.Y. 10007.

INDUSTRIAL/COMMERCIAL

ANNOUNCEMENTS ANNOUNCEMENTS ANNOUNCEMENTS

UNITED STATES BANKRUPTCY COURT FOR THE WESTERN DISTRICT OF TEXAS AUSTIN DIVISION

IN THE MATTER OF

COUNTRY JUNCTION, INC., f/k/a L. & M. HOUSE OF JEANS, INC. AND JUNCTION/HOUSE OF JEANS, INC.,

DEBTOR

CASE NO. L-81-00473 E

IN PROCEEDINGS FOR REORGANIZATION UNDER CHAPTER 11 OF THE BANKRUPTCY CODE

(JOINTLY ADMINISTERED)

SOLICITATION TO BID ON LEASES

NOTICE IS HEREBY GIVEN that on the 21st day of March, 1982, in Courtroom #1, U.S. Bankruptcy Court, on the 3rd floor of the United States Post Office Building, 615 E. Houston Street, San Antonio, Texas, at 9:30 A.M., COUNTRY JUNCTION, INC., et al (collectively), the Debtors-in-Possession herein, will receive and consider all bids, oral and written, made for the disposition of the Debtor's rights under any or all of the following Leases, to which the Debtors are a party:

LOCATION:	STORE SIZE:
Frederick Town Mall	6,000 sq. ft.
Frederick, Md. 21701	
Laddover Mall	2,000 sq. ft.
Laddover, Md. 20785	
Valley Mall	3,840 sq. ft.
Hagerstown, Md. 21740	
University Mall	2,520 sq. ft.
Blacksburg, Va. 24060	
Tanglewood Mall	2,200 sq. ft.
Roanoke, Va. 24014	
Mall at Manassas	4,200 sq. ft.
Manassas, Va. 22110	
Tower Mall	4,915 sq. ft.
Portsmouth, Va. 23702	
Park City Mall	4,900 sq. ft.
Lancaster, Pa. 17601	
Sogul Mall	2,275 sq. ft.
1165 King Street	
Alexandria, Va. 22314	
Beltline Mall	3,014 sq. ft.
1601 Beltline Rd. S.W.	
Decatur, Al. 35601	
Harrisburg East Mall	3,850 sq. ft.
Harrisburg, Pa. 17112.	
Riverside Mall	3,000 sq. ft.
Utica, N.Y. 13501	
Meadowville Mall	4,500 sq. ft.
Meadowville, Pa. 15146	
Newmarket North Mall	4,771 sq. ft.
Hampton, Va. 23602	
West Farms Mall	3,000 sq. ft.
Farmington, Ct. 06032	
Dentford Mall	5,770 sq. ft.
Dentford, N.J. 08000	
Millcreed Mall	2,070 sq. ft.
Erie, Pa. 16565	
Oakdale Mall	5,063 sq. ft.
Johnson City, N.Y. 13790	
Military Circle Shopping Center	4,500 sq. ft.
Norfolk, Va. 23502	
Pennsylayne Mall	3,630 sq. ft.
Lynchburg, Va. 24501	
Pembroke Mall	3,300 sq. ft.
Virginia Bch., Va. 23462	
LaVale Plaza	1,500 sq. ft.
LaVale, Md. 21502	approx.
Bristol Mall	2,700 sq. ft.
Bristol, Va. 24201	
Fort Henry Mall	4,000 sq. ft.
Kingsport, Tn. 37664	
Crossroads Mall	3,000 sq. ft.
Roanoke, Va. 24012	
Bowdoin Street Mall	2,154 sq. ft.
Winchester, Va. 22601	
Tysons Station	25,000 sq. ft.
7916 Leesburg Pike	
Falls Church, Va. 22043	
Congressional Plaza	15,000 sq. ft.
1601 Rockville Pike	
Rockville, Md. 20852	
Wedd'field Commerce Shopping Center	15,750 sq. ft.
1231 East Golf Road	
Schaumburg, Ill. 60195	
3652-P Peachtree Rd., N.E.	10,500 sq. ft.
Atlanta, Ga. 30319	
Old Keene Mill Shopping Center	9,045 sq. ft.
8330-C Old Keene Mill Rd.	
Springfield, Va. 22152	
Pixley Square	8,000 sq. ft.
1524 Butterfield Rd.	
Downers Grove, Ill. 60515	
Greenbr Shopping Center	10,000 sq. ft.
7483 Greenbelt Rd.	
Greenbelt, Md. 20770	
719 Southwest Military Dr.	5,000 sq. ft.
San Antonio, Tx. 78206	
Westgate Mall	3,500 sq. ft.
Austin, Tx. 78701	
Midtown Mall	3,000 sq. ft.
Killeen, Tx. 76541	
Governor's Mall	1,625 sq. ft.
Tallahassee, Fl. 32302	
Panama City Mall	3,757 sq. ft.
Panama City, Fl. 32401	

LOCATION:	STORE SIZE
Shepherd Mall	1,725 sq. ft.
Oklahoma City, Ok. 73116	
Cordova Mall	1,210 sq. ft.
Pensacola, Fl. 35202	
Memorial City Mall	3,300 sq. ft.
Houston, Tx. 77002	
Sharpstown Mall	2,000 sq. ft.
Houston, Tx. 77002	
Bel Air Mall	3,000 sq. ft.
Mobile, Al. 36601	
McCain Mall	2,500 sq. ft.
Little Rock, Ak. 72201	
Village Fair Mall	1,240 sq. ft.
Meridian, Ms. 39301	
Northlinc Mall	1,815 sq. ft.
Houston, Tx. 77002	
Westgate Mall	3,651 sq. ft.
Abilene, Tx. 79604	
South Park Mall	1,887 sq. ft.
Shreveport, La. 71101	
Hulen Mall	2,134 sq. ft.
Ft. Worth, Tx. 76101	
Town East Mall	4,000 sq. ft.
Mesquite, Tx. 75149	
Irving Mall	4,472 sq. ft.
Irving, Tx. 75060	
Hammond Mall	3,600 sq. ft.
Hammond, La. 70401	
Bon Marche Mall	2,852.48 sq. ft.
Baton Rouge, La. 70821	
Richardson Square	2,703 sq. ft.
Richardson, Tx. 75080	
Sher-Den Mall	4,294 sq. ft.
Sherman, Tx. 75090	
Red Bird Mall	2,954 sq. ft.
Dallas, Tx. 75231	
Northeast Mall	2,591 sq. ft.
Hurst, Tx. 76053	
Ridgemar Mall	2,339 sq. ft.
Ft. Worth, Tx. 76101	
Lake Air Mall	2,500 sq. ft.
Waco, Tx. 76701	
Sooner Mall	3,915 sq. ft.
Norman, Ok. 73069	
Broadmoor Mall	2,593 sq. ft.
Hobbs, N.M. 88240	
Mellor Park Mall	2,400 sq. ft.
El Dorado, Ak. 71730	
River Hills Mall	3,183 sq. ft.
Kerrville, Tx. 78028	
South Roads Mall	3,000 sq. ft.
Tulsa, Ok. 74101	
Woodland Hills Mall	1,773 sq. ft.
Tulsa, Ok. 74101	
Metro Center	3,210 sq. ft.
Jackson, Ms. 39209	
North Oaks Mall	2,250 sq. ft.
Houston, Tx. 77090	
Greenville Mall	2,400 sq. ft.
Greenville, Ms. 38701	
Central Mall	4,500 sq. ft.
Lawton, Ok. 73501	
Big Town Mall	2,753 sq. ft.
Mesquite, Tx. 75149	
Forum 303 Mall	4,500 sq. ft.
Arlington, Tx. 76010	
Town City Mall	1,120 sq. ft.
Monroe, La. 71201	
Indian Mall	3,000 sq. ft.
Jonesboro, AR. 72401	
Prestonwood Mall	3,645 sq. ft.
Dallas, Tx. 75201	
Golden Triangle Mall	2,863 sq. ft.
Denton, Tx. 76201	
Sikes Center	3,971 sq. ft.
Wichita Falls, Tx. 76307	
Crossroads Mall	2,479 sq. ft.
Oklahoma City, Ok. 73109	
Fayetteville Mall	2,541 sq. ft.
Fayetteville, Ak. 72701	
Leigh Mall	2,750 sq. ft.
Galveston, Tx. 77550	
North East Mall	3,000 sq. ft.
Hurst, Tx. 76053	
Heartland Mall	3,000 sq. ft.
Brownwood, Tx. 76801	

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[illegible] PRIOR TO THE DISPOSITION OF ANY LEASE IS SUBJECT TO FINAL AND SPECIFIC APPROVAL BY THE UNITED STATES BANKRUPTCY COURT FOR THE WESTERN DISTRICT OF TEXAS, WHICH APPROVAL WILL BE SOUGHT UPON NOTICE TO THE AFFECTED LANDLORD AND PARTIES IN INTEREST AT A HEARING TO BE SCHEDULED BEFORE THE HONORABLE JOSEPH C. ELLIOTT, JUDGE, U.S. BANKRUPTCY COURT. Any objection made to the disposition of a particular Lease shall be heard by the Court at that time.

Interested persons may submit bids or request additional information for any or all of the Leases prior to March 25, 1982, by contacting Stone-East Associates, Inc., agent for the Debtors: Attention Dean S. Golinsky, 40 West 57th Street, New York, New York 10019, (212) 977-9160.

All offers are subject to the terms and conditions set forth below:

1. A deposit of the greater of (a) ten percent (10%) of the offering price or (b) $3,000.00 shall be made payable to the order of COUNTRY JUNCTION, INC., Debtor-in-Possession, upon the Debtor's oral acceptance of an offer; such deposit to be made by check subject to collection. Such acceptance is subject to court approval as described above. The balance of the offering price shall be paid by bank or certified check within three (3) business days of the entry of an order of the Bankruptcy Court approving the consumption and disposition of the Lease.

2. The successful bidder shall enter into a "Purchase Agreement for Leasehold Interest" (hereinafter the "Purchase Agreement") upon the Debtors' oral acceptance of an offer. The Purchase Agreement can be obtained from Stone-East Associates, Inc. The provisions of the Purchase Agreement shall constitute additional terms and conditions of disposition.

3. Except as otherwise provided in the Purchase Agreement, in the event that COUNTRY JUNCTION, INC. does not, for any or no reason, consummate the disposition transaction, its sole liability to the successful bidder shall be for the return of bidder's deposit.

4. The Debtors reserve the right to reject any bid or bids which in their discretion are deemed inadequate or insufficient or which are contrary to the best interests of the estates of the Debtors and their creditors.

5. The disposition of a Lease does not include the sale of fixtures and equipment unless otherwise stated on March 25, 1982.

6. Prior to the bidding on each Lease on March 25, 1982, further specific details may be announced, including the establishment of upset prices for particular Leases.

7. No disposition is final until a Court Order is signed by the Bankruptcy Judge after notice to the affected Landlord and other parties in interest and hearing.

8. All bidders acknowledge that they have had an opportunity to review the Purchase Agreement, the Leases and all other pertinent documents in the possession of the Debtors or their agents regarding the Leases prior to making their offers and are relying on such review and their own inspection of the leasehold property in making their offers.

9. All sales and transfer taxes, recording fees, etc., if any, related to the disposition of the Leases shall be the sole responsibility of the successful bidders and shall be paid to the Debtors or the appropriate agent which due.

10. Country Junction reserves the right to dispose of any Lease by private sale or otherwise prior to March 25, 1982.

NOTICE IS FURTHER GIVEN that the Debtors may, in their discretion, withdraw any of the above-referenced Leases from competitive bidding from time to time or may adjourn the consideration of bids thereof, without notice to creditors or other parties in interest, other than by announcement of such withdrawal or adjournment on the dates scheduled for hearing.

DATED: March 9, 1982.

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May 12, 1982

MEMORANDUM

TO: William C. Lucius, Douglas B. Comer
Arthur B. Briskman, Barry Bauman

FROM: Paul C. Fiduccia

SUBJECT: Data on Shopping Center Tenant Bankruptcy

You requested that we provide data on the magnitude of the problem of shopping center tenant bankruptcies.

Unfortunately, such data is not currently available. Unlike the situation regarding personal bankruptcies, where a few large retailers may have had bankruptcy data generated in the normal course of their business, most of ICSC's shopping center developer members are small businesses with one to six shopping centers.

While ICSC has not done a survey of all of its members to determine their experience under the Bankruptcy Code, recently it has surveyed a number of shopping center developers, tenants, and bankruptcy attorneys who have expressed an informed opinion that the problem of bankrupt tenants is extensive in the industry and is growing. There are indications that a substantial percentage of shopping centers have had at least one tenant bankruptcy under the Code.

Earlier data would have limited relevance because shopping center tenant bankruptcies appear to have become a serious problem only in the last year. Therefore, in order to answer your questions, it has been necessary to use various aggregate data, estimates and assumptions.

Based on the data available and the assumptions made, our conclusions are as follows:

1. Prior to the enactment of the Bankruptcy Reform Act of 1978, shopping centers had limited problems with tenant bankruptcies because most leases provided for the termination of a lease in the event of a tenant bankruptcy.

2. Since the enactment of the 1978 Act, virtually all bankruptcies of shopping center tenants have presented problems to shopping center landlords and non-bankrupt tenants.

a. In 1981, there were 22,750 shopping centers in the U.S. Approximately 40% of all retail firms and 42% of all U.S. retail trade are in shopping centers.

b. Approximately 85% of new establishments of national department stores and other chain retailers are going into shopping centers.

c. Approximately 12% of all new shopping center construction is in downtown areas.

d. The percentage of retail trade conducted in shopping centers and the percentage of shopping centers in downtown areas is increasing.

e. The total number of retail establishments in shopping centers is approximately 1,255,000.

f. Conservatively estimated, approximately 16,985 stores in 14,770 shopping centers were involved in bankruptcies in 1981; this involved approximately 65% of all shopping centers.

g. Continued economic problems may result in a greater number of affected shopping centers in 1982.

ANALYSIS

I. Retail and shopping center industry profile

A. Retail Firms and Establishments1/

1. 1977 firms and establishments:

a. total firms; 1,567,071; total establishments; 1,855,068.

b. single unit firms; 1,523,371; single unit establishments; same.

c. multi-unit firms; 43,700; multi-unit establishments; 331,697.

2. Multi-unit (chain) firms (1977) as a percentage of total firms: 2.79%.

B. 1981 Retail Trade

In 1981, 22,750 shopping centers did approximately 42% of all U.S. retail trade. Because shopping center tenants include most of the larger retailers, this amount of retail trade is transacted by approximately 40% of all retail firms. The percentage of U.S. retail sales made in shopping centers, the percentage of retail firms located in shopping centers, and the percentage of shopping centers located in downtown areas are increasing.

C. Categories of Shopping Centers and Number of Stores in Shopping Centers.

1. Categories:

For statistical purposes, shopping centers can be put in four categories:

a) Super-Regional, with an average of 130 stores and 750,000 or more square feet of Gross Leasable Area (GLA),

b) Regional with an average of 95 stores amd 400,000 or more square feet of GLA,

c) Community with an average of 50 stores and 150,000 or more square feet of GLA, and

1/ Source: 1977 Census of Retail Trade, Table B-Subject series establishment and firm size; 1981 Department of Commerce Retail Sales Figures.

d) Neighborhood with an average of 30 stores and 25,000 or more square feet of GLA.

Approximately 75% of all shopping centers (approximately 17,000) are Community and Neighborhood shopping centers.

2. Assumptions:

a) Of the 17,000 Community and Neighborhood shopping centers, half are Community and half are Neighborhood with a combined average number of 40 stores per shopping center;

b) Of the Super-Regional and Regional shopping centers, half are Super Regional and half are Regional with a combined average number of 100 stores per shopping center;

3. Conclusions based on these assumptions:

a) Stores in Community and Neighborhood centers: 680,000 (17,000 x 40);

b) Stores in Super-Regional and Regional centers: 575,000 (5750 x 100);

c) Total stores in all shopping centers; 1,255,000 (680,000 + 575,000).

D. Percent of Gross Leasable Area by Type of Stores and Type of Shopping Center:

1. Category and Area

Shopping Center	% of GLA Occupied2/ by National Stores (multi-establishment)
Super Regional	79.8
Regional	71.6
Community	61.5
Neighborhood	46.3

2. Estimated percentage of shopping center leasable area occupied by national (chain) stores: 60%.

3. Note: There are no reliable statistics on the percentage of shopping center tenants which are regional or local chains. Therefore, we have assumed that all non-national

2/ Dollars and Cents of Shopping Centers: 1981, The Urban Land Institute.

stores are single establishment firms, recognizing that this assumption tends to understate the magnitude of the bankruptcy problem by reducing the estimate of affected establishments.

II. Impact of Bankruptcy on Shopping Center Tenants

A. Dunn & Bradstreet (D&B) data on the number of business failures.[3/]

There were 3278 reported retail firm failures in the first 6 months of 1981. We estimate that the total retail firm failures in 1981 was 7146. This assumes that the rate of increase of retail failures from the first 6 months of 1980 to the first 6 months of 1981 (18%) continued from the first 6 months of 1981 to the last 6 months of 1981, resulting in 3868 retail business failures in the second half of 1981, for a total of 7146 failures in 1981.

B. Administrative Office of U.S. Courts (AOC) data on business bankruptcies.[4/]

1. Business bankruptcies

Business Bankruptcies	Total	Merchants
Calendar 1981	66,259	-
Calendar 1980	60,161	-
Year ending 6/30/79	29,500	4,306 (15%)
Year ending 6/30/78	30,528	5,759 (19%)
Year ending 6/30/77	32,189	6,881 (21%)

2. Assumptions and Conclusions

If it is assumed that the percentage of total business bankruptcies which were of merchants has remained unchanged since June 30, 1979 (15% of total), then there would be 9900 bankruptcies of merchants in 1981 (15% of 66,259).

C. Estimates of total retail trade firm bankruptcies in 1981.

1. Based on D&B's data: 7146.

2. Based on the AOC's data: 9900.

3/ Business Economic Division, March 18, 1982 Release.

4/ Telephone conversation with Mr. Kimmel; Bankruptcy Division, May 5, 1982.

3. ICSC estimate, 8500 firms (average of D&B and AOC data).

D. Estimated shopping center establishments involved in and shopping centers affected by bankruptcies.

1. Retail trade firms bankrupt in 1981; 8500 (average of D&B and AOC data).

2. Multi-establishment retail firms bankrupt in 1981: 237 (2.79% of 8500).[5/]

3. Multi-establishment retail firms bankrupt in 1981 with stores in shopping centers: 95 (40% of 237).[6/]

4. Shopping centers stores of multi-establishment retail firms bankrupt in 1981: 13,680 (144 x 95).[7/]

5. Non-multi-establishment retail firms, bankrupt in 1981, in shopping centers, 3305 (3400 - 95).[8/]

6. Total establishments involved in bankruptcies in 1981 located in shopping centers, 16,985 (13,680 + 3,305).

7. Total shopping centers affected by the bankruptcy of a tenant in 1981, 14,770 (assume 85% of shopping centers with a bankrupt tenant have only one bankrupt tenant, and the remaining 15% have two bankrupt tenants).

8. Percentage of shopping centers affected by a tenant bankruptcy, 65% (14,770 ÷ 22,750).

9. 1982 Impact: Current news reports and other information indicate that 1982 retail bankruptcies may exceed 1981 bankruptcies.

5/ Assumes that multi-establishment firms went bankrupt at the same rate as single-establishment firms.

6/ Assumes that multi-establishment firms with stores in shopping centers went bankrupt at the same rate as multi-establishment firms without stores in shopping centers.

7/ An October 1980 ICSC survey on shopping center retail firm expansion plans showed that of 466 responding, there were an average of 180 establishments per firm. Assuming that 80% of these establishments were in shopping centers, each would have 144 establishments in shopping centers. ICSC surveys show that today 85% of new establishments of chain stores are in shopping centers.

8/ Assumes all non-national firms are single-establishment firms. This assumption significantly understates the number of affected stores.

PREPARED STATEMENT OF HOWARD C. OLIVER

My name is Howard C. Oliver. I am Senior Vice President of Finance and Operations of Jim Wilson & Associates, Inc., a Montgomery, Alabama based real estate development company specializing mainly in the development of regional shopping center malls throughout the sunbelt area of the United States. Included among my current responsibilities is the operation of twelve regional malls and five strip centers in North Carolina, South Carolina, Florida, Georgia, Mississippi and Texas. As such, I have overall responsibility for tenant relationships and the operation of the properties. Prior to joining Jim Wilson & Associates, I was an attorney with the firm of Hobbs, Copeland, Franco & Screws in Montgomery, Alabama.

As Congress recognized in enacting the Bankruptcy Code, shopping centers are a unique type of real estate arrangement. The success of each tenant is dependent in major part upon the activities of the other tenants. The activity of primary importance is the vigorous operation by the other tenants of businesses carefully selected to contribute to a desired tenant mix. A proper tenant mix is essential to attract a sufficient number of customers to justify the higher costs of operating a store in a shopping center.

Accordingly, shopping center leases are unique among all leases of real property in that each lease arrangement involves not only the interests of that tenant and the landlord, but also involves the interests of every other tenant of the shopping center. This commonality of interests is reflected in clauses which specify the business use permitted in each tenant's premises, which specify that tenant space is to be fully operated, and which specify other required and prohibited actions designed to further the interests of the shopping center as a whole.

Under the Bankruptcy Act prior to 1978, the interests of the shopping center and its other tenants were protected in the event of the bankruptcy of a tenant by various lease clauses allowing the landlord to regain control of the premises. The enactment of the Bankruptcy Reform Act of 1978 (the Code) made such clauses unenforceable. However, Congress recognized the special problems of shopping centers and their tenants, and included in the Code special protections regarding the assumption and assignment of shopping center leases.

Unfortunately, these protections have not worked as intended by Congress. The requirements that specific assurances of future performance under the lease be made have been applied in ways that provide little actual protection to shopping centers and their tenants.

The purpose of this bill is to make the protections enacted in 1978 effective. The practical effect of the changes proposed in this bill is to make clear the intent of Congress in 1978 to protect the interests of shopping centers and their tenants and to prevent the detrimental economic impact of the bankruptcy of a tenant on the nonbankrupt tenants and the shopping enter. This is accomplished primarily by shifting various procedural burdens which currently work against the shopping center and the solvent tenants.

In my testimony today, I would like to emphasize three of the most serious problems encountered by shopping centers under the Bankruptcy Code and to discuss the remedies to these problems which this bill proposes. These problems are serious and affect many shopping centers, including ours. Indeed, these are among the most serious problems experienced by Jim Wilson & Associates in the operation of their shopping centers.

The first problem is the open ended and often lengthy delays in the decision by the trustee or debtor-in-possession to assume or reject a shopping center lease. This often results in

an extended period when a store is vacant, and this hurts the business of the other tenants and forces the shopping center and the other tenants to bear some of the costs of the bankruptcy.

The second problem is the failure of the trustee or debtor-in-possession to pay current rent and other charges during these long periods of delay. This practice is particularly injurious in the case of small shopping centers where the revenues from a major tenant may be essential for the landlord to pay mortgage and tax payments as they become due; the failure to make such payments may endanger the operation and existence of the shopping center and the solvent tenants.

The third problem is the assignment of the shopping center leases of bankrupt businesses to other businesses in violation of the use clause of the lease. This also harms the shopping center and its other tenants, and where a major tenant's space is involved can be disastrous.

I believe that none of these consequences is justified on any policy basis. Also I do not believe that Congress intended these consequences when the Bankruptcy Code was amended in 1978, especially in light of the fact that Congress specifically provided protections for shopping center leases in section 365(b)(3) of the 1978 Amendments.

I am here today to urge this Subcommittee to remedy these and other problems in the implementation of section 365 of the Code, and to provide the proper balance between the interests of the debtor and the interests of the shopping center and its other tenants. The protections which Congress intended to provide us in 1978 have not worked--they need to be improved. S. 2297 would accomplish this improvement.

SUBSTANTIAL AND UNJUSTIFIED DELAYS IN DECISION TO ASSUME OR REJECT LEASE

Substantial delays are currently experienced under the

Code in the decision by the trustee or debtor-in-possession to accept or reject the lease of the tenant space. Our experience has been that significant and unnecessary delays are commonplace under current bankruptcy proceedings. These delays are injurious to the financial well being of both owners and other tenants in shopping centers.

We have experienced delays of from four to six months in regaining the possession of premises from tenants who have terminated business operations, stopped paying rent and other charges, and filed a petition in bankruptcy. This problem is further aggravated by the fact that in many cases the bankruptcy petition was filed several months after the tenant vacated the premises and defaulted on his lease. During this extended time period we are unable to release the premises to a viable tenant.

For example, Jim Wilson & Associates had six executory leases outstanding with a store doing business as "The Junction." In September, 1981, several of these locations were boarded up by the tenant. We attempted for several months to obtain the possession of the premises so that the property could be leased to operating businesses. In December, 1981, the tenant filed a bankruptcy petition, thus automatically staying all matters relating to the various premises. It was not until April, 1982, that the leases were rejected, with the result that a period of eight months passed during which the space was not occupied and operated. Because it was uncertain when, if ever, the premises would be available for releasing, it was difficult to negotiate a lease with a new tenant until the lease was rejected. Consequently, there was an additional delay in releasing the space after the lease was rejected.

Jim Wilson & Associates has been most fortunate in not having a major tenant or anchor tenant go bankrupt in any of our existing properties. However, we have managed properties where the anchor stores were closed due to bankruptcy and other causes,

and we have witnessed the damaging effects of such closings on the landlords and tenants in those shopping centers. The most serious adverse effects have been on the smaller tenants of shopping centers where an anchor store was closed. For example, in one Texas mall which we own, a major tenant was approximately seven months late in opening. While the mall was generally successful, four tenants experienced some financial difficulty, and three of the four were located in the immediate vicinity of the one department store which was not open for business.

Due to the nature and design of most shopping centers, it is extremely important that the major tenants be open and operating for business. Operating anchor stores are necessary to attract customers to the mall, and these customers are necessary for the small tenants to be successful. Our experience is that if a major store is not operating, the immediately adjacent small tenants can experience extreme financial difficulty due to decreased sales volumes caused by the reduced traffic. This is particularly a hardship on local merchants who do not have the strong capital base of some chain stores. In difficult economic times such as these, any unnecessary delay in the reopening of major mall tenants could be disastrous to the smaller tenants. Unfortunately, the Code routinely permits and facilitates such delays.

FAILURE TO PAY CURRENT RENT AND OTHER CHARGES

The second problem we have had under the Code is related to the problem described above. During the lengthy delays between the closing of a store and the decision by a trustee or debtor-in-possession to assume or reject the lease, payments for rent and other charges (such as common area maintenance costs) are often not paid. This is particularly a problem where the premises are not being operated and the debtor has little hope of a successful reorganization.

In the bankruptcy of "The Junction" described above, payments for rent and other charges were not made for a period of several months. We were thus required to provide the use of our property and other services to the estate of the debtor with no current compensation. We are not aware of any other class of creditor which is required to provide a benefit to the bankrupt's estate without current compensation.

In addition, in the event that the lease is ultimately rejected, the landlord can expect only a small fraction of the unpaid rent and charges on disposition of the case.

ASSIGNMENT OF LEASES TO BUSINESSES NOT IN CONFORMANCE WITH USE CLAUSES--DISRUPTION OF TENANT MIX

The third serious problem we have encountered under the Code relates to the proposed assignment of shopping center leases by a tenant in a bankruptcy proceeding. For the conscientious and successful landlord, a great deal of time, effort and expertise is devoted to achieving the "right" tenant mix in the shopping center. The right mix is essential to the success of the shopping center and each of its tenants. This tenant mix and the traffic it attracts is what the tenants in a shopping center are buying when they go into a center.

In some cases an immediate financial advantage to the debtor can be obtained through the assignment of a property to the person who offers the highest price, regardless of his business. However, experience has shown that a proper mix of tenants and merchandise must be available in the center to avoid reducing the revenues of all the tenants, especially those whose market may become overloaded through a lease assignment to another tenant in the same business. Thus, what may appear to benefit the debtor in the short run may have a serious economic impact on the solvent tenants in the shopping center.

In the most recent instance of this problem in our

experience, the trustee proposed to assign the lease to a type of store of which there were already two in the mall, even though such an assignment would violate the use clause of the lease. No consideration was given to the fact that the landlord would under no circumstances have rented to the proposed assignee because of the negative impact such an act would have on the two existing merchants in the same line of business and on the other tenants because of the impact of such action on the traffic in the shopping center. The sole criteria of the trustee was the generation of the most money for the bankrupt estate, regardless of the consequences to the shopping center and its other tenants.

It is important to the health of the shopping centers and their tenants, a major sector of U.S. retail trade, that Congress change the Code to insure that when a specific and definite use for the premises is required under a shopping center lease, any assignment must be in conformance with the use clause.

CONCLUSION

When Congress made unenforceable lease clauses permitting shopping center landlords to regain control of the space of bankrupt tenants in 1978, it sought to protect shopping centers and their other tenants from the adverse consequences of such a limitation by including specific protective language in the Code. The goal was to provide an equitable balance between the interests of the shopping centers and their tenants and the interests of debtors. The problems I have described are caused by unintended imbalances in the interests of these parties created by the Code.

The problem of delay should be remedied by requiring the trustee or debtor-in-possession to assume or reject the lease within 60 days, unless he can show cause to the court for more time.

The problem of failure to pay rent and other charges on

a current basis should be remedied by requiring the debtor to perform its obligations under the lease on time.

The problem of the assignment of a lease to non-conforming businesses use, and the consequent problem of disrupting the tenant mix, should be remedied by removing the word "substantially" from the provisions dealing with adequate assurances that use clauses will be honored and tenant mixes not disrupted.

I urge the subcommittee to adopt these charges and the other proposals contained in S.2297 and to support their expeditious enactment into law.

PREPARED STATEMENT OF GEORGE LAMBROSE

My name is George Lambrose. I am the Managing Partner and Owner of the Southgate Mall, located in Missoula, Montana. The Southgate Mall is a 650,000 square foot shopping center with 4 department stores and 91 smaller shops. I have been in the shopping center business for 22 years, and have owned the Southgate Mall for 4 years.

I am testifying this morning in support of S. 2297 because this bill would remedy problems created by the Bankruptcy Reform Act of 1978 (the Code). These problems are serious and have already damaged the business of many shopping centers and many more tenants.

One of the changes which this bill would make would be to delete the word "substantially" from provisions in the Code which require that the trustee or debtor-in-possession make assurances regarding conformance with the use clauses of the lease and the disruption of the shopping center's tenant mix. The need for this change is at the same time extremely important and somewhat difficult to explain. Since other witnesses here this morning will be testifying regarding the other provisions of this proposal, I will confine my comments to this one issue.

Section 365 of the Bankruptcy Code provides that adequate assurances of future performance under an unexpired shopping center lease must be made in order for the trustee or debtor-in-possession to assume or assign such a lease. Section 365(b)(3)(C) provides that adequate assurance of future performance under the lease must include "that assumption or assignment of such lease will not breach substantially any provision, such as a radius, location, use, or exclusivity provision..." Section 365(b)(3)(D) provides that an assurance must also be made "that assumption or assignment of such lease will not disrupt substantially any tenant mix or balance in such shopping center."

These provisions were intended by Congress to protect the business of the shopping center and all of its solvent tenants from being disrupted by the bankruptcy of a tenant. I cannot emphasize too strongly the importance of achieving and maintaining a proper tenant mix for a shopping center. Where this tenant mix is disrupted, even slightly, at a minimum the business of other tenants may be seriously jeopardized. Where the use clause is not followed in the case of the assignment of an anchor store lease, especially in a strip center with only one such store, the effect on the shopping center can be devastating.

Although it might seem that a requirement that use clauses be substantially complied with and that the tenant mix not be substantially disrupted would provide protection against these harms, this is not the case for two reasons. First, bankruptcy referees in court uniformly pursue a policy of interpreting the Bankruptcy Code in a way that will benefit the estate of debtors. For this reason, an attempted assignment of a shopping center lease to a business not in conformance with the use clause will be presumed acceptable.

Second, even if the referee or bankruptcy court attempts to apply the law in an evenhanded manner, it is virtually impossible to convince such decisionmakers of the care with which business uses are selected and the amount of harm which can result from apparently minor differences in the business use of the original tenant and the potential assignee.

I have appended to this statement as an exhibit, documents which I use in my mall to determine the proper tenant mix. As you can see from these documents, determinations of appropriate businesses for the mall are not made on a haphazard or informal basis. Experience has shown that successful shopping centers must be carefully planned, and that that plan must be implemented. It is better to receive a lower rent from a business which contributes to the tenant mix rather than a higher rent from a business which does not.

99-782 O—82——5

In this exhibit, you will see that the businesses in the mall are balanced by categories of business and within each category, subcategories are specified by quality range.

The percentages of total floor space allocated to each category of merchant is periodically compared to the percentage of total mall sales from each category. As a result of these comparisons, these percentages are adjusted to "fine tune" the mall for optimum performance.

As you can see, appropriate uses for mall space are determined with a high degree of precision. Once a correct mix has been established, the landlord does whatever possible to maintain it. For example, a company owning a chain of pizza restaurants filed for bankruptcy last year. I determined that it was in the best interests of the mall and its other tenants that there be such an establishment in the mall. Accordingly, I negotiated with the creditors of the pizza parlor, with persons who had made personally guarantees on the lease, and with a potential assignee of the premises to continue operation there. Fortunately, these negotiations were successful, the pizza parlor remains in operation, the tenant mix has been preserved.

It is important to note that deleting the word "substantially" from these provisions would in no way prevent the assignment by debtors of their leases. Although shopping center lease use provisions are drawn with various degrees of specificity, even the narrowest use description still covers a market segment served by a very large number of existing and potential businesses. Although requiring strict performance of the use clause of the lease will limit the universe of potential assignees of any shopping center lease space, this limitation is absolutely necessary for the health of the shopping center and its other tenants and does not place an unreasonable burden on the debtor.

In conclusion, I urge the Subcommittee to approve

S. 2297 and I hope that this legislation may be enacted into law as soon as possible. Each of the proposals in that bill is needed by shopping centers and their tenants. One of the most important of these changes would be to require that the use clauses in shopping center leases be precisely adhered to and that no disruptions of shopping center tenant mixes occur.

Thank you for your consideration of my views.

SOUTHGATE MALL TENANT
MIX ANALYSIS

MARCH 7, 1982

CATEGORY	SQ. FT. AREA	AREA %	NO. OF STORES	NO. OF STORES (PERCENT)
SHOES				
Proposed	(24,286)	(10.0%)		
Actual	20,594	8.48%	8	9%
JR. DEPT. STORES				
Proposed	(19,428)	(8.0%)		
Actual	17,538	7.22%	1	1%
WOMENS RTW				
Proposed	(48,572)	(20.0%)		
Actual	48,939	20.15%	16	17%
SPECIALTY RTW				
Proposed	(7,285)	(3.0%)		
Actual	6,268	2.58%	4	4%
MEN RTW				
Proposed	(29,143)	(12.0%)		
Actual	32,100	13.21%	8	9%
JEWELERY				
Proposed	(7,285)	(3.0%)		
Actual	6,932.70	2.85%	5	5%
GIFT				
Proposed	(21,857)	(9.0%)		
Actual	21,113.10	8.69%	7	8%
FOOD				
Proposed	(29,143)	(12.0%)		
Actual	34,681	14.28%	17	18%
HOUSEHOLD				
Proposed	(9,714)	(4.0%)		
Actual	4,250	1.75%	1	1%
SEASONAL & MISC.				
Proposed	(41,285)	(17.0%)		
Actual	41,391	16.67%	19	20%
NON RETAIL				
Prposed	(4,857)	(2.0%)		
Actual	5,153	2.12%	4	4%
VACANT				
Actual	4,862	2%	3	3%
TOTAL PROPOSED	242,923.80	100%	93	100%
TOTAL LEASED	238,061.80	98%		

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March 7, 1982

SOUTHGATE MALL

TENANT MIX EVALUATION - 1982

TENANT	AREA	%
SHOES		
Proposed	24,292	10.0%
Actual	(20,594)	(8.48%)
Gallenkamp Shoes	3,432	
Kinney Shoes	3,360	
Naturalizer Shoes	1,099	
Ogg's Shoes	3,650	
Thom McAn Men's	1,205	
Thom McAn Women's	2,645	
Baker Shoes	2,500	
Footlocker	2,433	
JR. DEPT. STORE		
Proposes	19,433	8%
Actual	(17,538)	(7.22%)
Place Two	17,538	
WOMEN'S R-T-W		
Proposed	48,585	20%
ctual	(48,939)	(20.15%)
Anita Shop	4,937	
The Closet	2,390	
Dahle's Queen&Tall	3,285	
The Daisy	1,065	
Foxmoor Casuals	1,825	
Jean Nicole	4,867	
Kay's Dress Shop	1,460	
Lerner Shop	5,988	
Maurice's	3,650	
Conrad's	2,738	
Peck & Peck	2,240	
Stevenson's	3,650	
Wardrobe	3,381	
Jay Jacobs	3,640	
The Altogether	1,708	
Jenny's Fashions	1,162	
SPECIALTY R-T-W		
Proposed	7287	3.0%
ctual	(6268)	(2.58%)
Dana's	898	
Shirt Works	976	
Motherhood Maternity	915	
Young Generation	3,479	
MEN'S R-T-W		
Proposed	29,150	12.0%
Actual	(32,100)	(13.21%)
Chess King	2,494	
Dahle's Big&Tall	3,305	
Kaufman's	6,000	
K-G Men's	5,723	
Mr. Mark	1,315	
Squire Shop	3,640	
Bo Legs	2,946	
Desmonds	6,677	

TENANTS	AREA	%
JEWELRY		
Proposed	7,288	3%
Actual	(6,932.70)	(2.85%)
Zales	1,470	
Don Davis Jewelers	1,367	
Edward Jewelers	1,460	
Morgan Jewelers	915.7	
Schubach Jewelers	1,720	
HOUSEHOLD		
Proposed	9,717	4%
Actual	4,250	(1.75%
House of Fabric	4,250	
FOOD		
Proposed	29,143	12%
Actual	34,681.1)	(14.78%
Baskin-Robbins	976	
Brandy's	1,249.5	
Bonaparte's	1,710	
Dairy Queen	372	
G.N.C.	2,218	
Gyros	735	
Hickory Farms	2,279	
Hol'n One	1,464	
J.B. Big Boy	2,691	
King's Table	6,188	
Lenny's Lounge	1,516.6	
Orange Julius	1,147	
Rafferty's Candies	766	
Slice-A-Pizza	1,525	
Pancho's	2,501	
Snickerdoodles	750	
Rocking Horse	6,593	
GIFTS		
Proposed	21,857	9%
Actual	(21,113.1)	(8.69%)
Gift Crate	1,033.4	
Hatch's	5,044	
Higgins Hallmark	4,910	
Magic Muchroom	3,420.7	
Garden City Floral	2,528	
Spencer Gifts	2,677	
Everything Under the Rainbow	1,500	
SEASONAL & MISC.		
Proposed	41,297	17%
Actual	(40,493)	(16.67%)
Bathtique	1,162	
Bell Pipe Shop	465	
Command Performance	1,962	
Merle Norman	366	
Regis Hairstylists	1,022	
State Optical	980	
Universal Athletics	1,487	
Smith Knife & Stone	457	

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SOUTHGATE MALL-TENANT EVALUATION page 2

TENANT	AREA	%
SEASONAL & MISC. continued		
B. Dalton	3,655	
Hi County	2,885	
Clowntown	2,518	
Western Sportsman	6,971	
Coles Books	3,611	
Hobby Shoppe	1,220	
Craft Creations	1,500	
Lowrey Organ Center	1,470	
Musicland	3,356	
Radio Shack	2,064	
Kay Bee Hobby & Toys	3,432	
NON-RETAIL		
Proposed	4,857	2%
Actual	(5,153)	(2.2%)
Lambros Realty	812	
Global Travel	405	
Alladin's Castle	2,716	
Phone Center Store	1,220	
VACANT SPACE		
Actual	(4,862)	(2%)
Vacant Space	1,125	
Vacant Space H3	2.433	
Vacant Singer Space	1,304	
TOTAL	242,923.80*	

*Does not include department stores.

PREPARED STATEMENT OF JOHN S. HOLMES, SR.

My name is John S. Holmes, Sr. I am the President of the Merchants Association of the Frederick Shopping Center, located in Frederick, Maryland. I own a store in that shopping center which sells delicatessen food and beverages. The Frederick Shopping center is an unenclosed "strip center" of approximately 25 stores. Most of these businesses are locally owned and family operated. The Frederick Shopping Center merchants are entrepreneurs who have joined together in this shopping center to promote their common interests.

As President of its Merchants Association, I am aware of the problems and concerns of all of the merchants doing business there. I have operated my store in the shopping center for 22 years, and have been President of the Merchants Association for 11 of those years. In all this time, the most serious problem that our shopping center has ever encountered has been caused by the bankruptcy and closing of two stores. One of these stores was a Food Fair grocery store which occupied a central location in the shopping center and provided the major drawing power to the shopping center. The other was an automotive parts and service establishment called Joe The Motorist.

The purpose of my testimony this morning is to explain the damage to the other tenants of the Frederick Shopping Center resulting from the closing of these stores and the inability of the shopping center to re-lease this space to operating businesses for a period of time. I also want to encourage the Subcommittee to amend the Bankruptcy Code to lessen these problems in the future as proposed in S. 2297.

BANKRUPTCIES IN THE FREDERICK SHOPPING CENTER

In Early 1980, Joe The Motorist filed for bankruptcy under chapter 11. This store continued to operate under chapter 11 until June 30, 1981. After terminating operations and boarding up its premises, this tenant attempted for several months to assign its lease to another business. It was

unsuccessful in this attempt and finally rejected the lease in March, 1982. Because of the uncertainty of whether or not the lease would be assigned, it was not possible for the shopping center to begin serious negotiations with another tenant until the lease was rejected. During that period I talked to two persons who were interested in leasing that space, but who could not lease it then. It was not until April that another tenant was located and operations resumed in that location.

A major store in the Frederick Shopping Center was a Food Fair grocery store. This store was in a central location in the shopping center and provided primary drawing power to all of the other tenants in the center. On July 31, 1981, the Food Fair store in the Frederick Shopping Center closed. In September of 1981, Food Fair assigned its lease to another grocery store, Farm Fresh. Farm Fresh opened for business on November 18, 1981.

In the case of the Joe The Motorist store, the shopping center tried to regain control of the lease so that the space could be re-leased to an operating business, but was unable to do so. In the Food Fair situation, the shopping center was also unable to regain the lease, but was fortunate in that Food Fair succeeded in assigning its lease to another grocery store approximately two months after closing.

I understand that much longer delays in reopening a closed store have been experienced in other shopping centers. If that is the case, I have difficulty understanding how other tenants in those centers survived. Even the comparatively short time the Food Fair store was closed severely damaged the business of many of the merchants of this shopping center, and in many cases the stores have not yet recovered.

IMPACT ON OTHER TENANTS OF MAJOR STORE CLOSINGS

Last week I talked to many of the other merchants in the Frederick Shopping Center about the affect of the store closings on their business. Every merchant with whom I spoke suffered a decrease in sales revenues over the period of the closings. For example, Kilbey's Appliances, which is next to the

Food Fair store location, suffered a sales drop of 28 percent. The Horn and Horn restaurant suffered a 26 percent reduction in sales. May's Hardware Store, Olin Mills, Sherwin-Williams Paints, Woolworth's, Peoples Drug Store and the barber shop had sales reductions of ranging from approximately 20 to 25 percent. Sales in my store decreased 18 percent over that period.

It is important to understand what sales reductions of this magnitude mean in human terms--they mean that people's jobs are in danger. Our center was fortunate in that new stores resumed operations before it was necessary to lay-off our employees.

For some of the stores in the shopping center, sales are just now returning to their levels prior to the store closings. Because of these returns to previous levels, we do not believe that the reductions I have just discussed were caused by the recession.

However, for some stores business has not returned to its previous levels. The closing of a major store (such as a Food Fair) in a shopping center forces customers to go to other locations. It is natural that once at another shopping center to purchase groceries at its operating food market those customers will then make other purchases from merchants in that center. When the prolonged closing of a major store forces this shifting of patronage to another center for a period of time, in this case almost 4 months, customers change their buying "traffic" patterns. Relationships are established with the merchants in the other shopping center which in some cases will be permanent. In other cases, the customers will come back, but this takes time.

NEED A PROPER BALANCE BETWEEN THE INTERESTS OF THE BANKRUPT TENANT, THE OTHER TENANTS, AND SOCIETY

As a shopping center tenant, I have a strong interest in Bankruptcy Code provisions which would enable me to reorganize my business if the need arose. Where tenants in our mall, such as Joe The Motorist, have continued to operate their store under chapter 11, the other tenants have not been significantly injured. However, when a tenant closes his store with no

intention or no prospects of reopening it, the other tenants are harmed to an extent far greater than any benefit to the bankrupt tenant. In addition, society as a whole is forced to pay the price of increased unemployment, reduced tax receipts, and reduced economic activity.

Although I understand that in some cases the assignment of a shopping center lease is a valuable asset of the debtor's estate, I believe it is improper for a bankrupt tenant to use the fact of his store's closing and the impact of that closing on the other tenants to his advantage.

All of the members of the Frederick Shopping Center Merchants Association understand that they may one day need the protection of the Bankruptcy Code. However, they are acutely aware that at this point we need protection <u>from</u> the Bankruptcy Code. We strongly urge that Congress amend the Code in ways that will minimize the time that the store of a bankrupt shopping center tenant may be closed. It is in the interest of all of the other tenants of the shopping center and of the shopping center landlord to reopen a closed location as soon as possible. Whatever benefits exist for debtors under the present law are far outweighed by the detriments to the rest of us in these situations.

IMPORTANCE OF COMPLYING WITH USE CLAUSE-- ESPECIALLY IN THE CASE OF A MAJOR TENANT

The other merchants in the Frederick Shopping Center were fortunate that Food Fair assigned its lease to another grocery store. Had that lease been assigned to <u>any</u> business other than a grocery store the negative effect on the shopping center would probably have been permanent and irreversible.

I cannot emphasize too strongly the fact that all of the other tenants of the Frederick Shopping Center depend upon the existence of a centrally located grocery store in the shopping center. In the absence of such a store, none of us would get the benefit of the bargain which we have with the shopping center landlord.

We pay shopping center rents which are higher than

rents we would pay for the same amount of space elsewhere because we understand that the drawing power of the grocery store, and of all of the other tenants, will provide traffic sufficient to pay these higher rents. The assignment of a lease to a business use other than that specified in the lease agreement, especially in the case of a major tenant, would be a disaster. It would completely eviscerate the agreement we have with the shopping center landlord and would quite likely cause substantial harm to the other tenants, and threaten their bankruptcies as well.

CONCLUSION

The merchants of the Frederick Shopping Center strongly support the changes which this bill would make in the Bankruptcy Code. These changes are necessary and in the view of tenants, who must view these changes from the perspective of persons who might need the protections of the Code, establish a fair balance of the interests of the bankrupt tenant and the other tenants in a shopping center.

I urge Congress to act on these proposals as soon as possible to avoid further unnecessary harm to shopping center tenants across the country.

I thank the Subcommittee for its consideration of my views.

Senator HEFLIN. Our next witnesses are a panel of bankruptcy lawyers: Mr. Nathan Feinstein of Philadelphia and Mr. Laurence D. Cherkis of New York. We are delighted to have you. Which one of you wants to go first?

STATEMENTS OF NATHAN B. FEINSTEIN, PARTNER, COHEN, SHAPIRO, POLISHER, SHIEKMAN & COHEN, PHILADELPHIA, PA.; AND LAURENCE D. CHERKIS, WACHTELL, LIPTON, ROSEN & KATZ, NEW YORK, N.Y., REPRESENTING THE INTERNATIONAL COUNCIL OF SHOPPING CENTERS

Mr. FEINSTEIN. Thank you, Senator. I am Nathan Feinstein, a Philadelphia lawyer.

Senator HEFLIN. What is the connotation of a "Philadelphia lawyer?"

Mr. FEINSTEIN. It goes back to the very famous case of Peter Zenger. You will remember that Peter Zenger was a printer in colonial New York, and the then Royal Governor in New York had him held for sedition for criticizing the Royal Governor. No New York lawyer was able to defend Zenger at the time; they felt jeopardized.

Andrew Hamilton, the then leading lawyer in the colonies and, incidentally, one of the architects of Independence Hall, came up from Philadelphia to New York, defended Zenger, and established in that case the idea of freedom of the press for all of the English-speaking world. Since that time, there has been the title "Philadelphia lawyer" applied to certain lawyers.

Senator HEFLIN. Well, I am delighted to know that America now knows the contemporary explanation of that term. Thank you. [Laughter.]

Go ahead, sir.

Mr. FEINSTEIN. Thank you, Senator.

EFFECTS OF DELAY IN ASSUMPTION OR REJECTION OF LEASES

I wanted to respond first, if I may, to a question that you asked two or three times, and I think in different ways, essentially dealing with time and how it works. There are really two sorts of questions you were asking: One, the time to get a decision on whether a debtor will assume or reject the lease. From the shopping center tenant perspective, it is, "How long will it take before I know whether that user is going to be there, because I have got to order my goods, my men's clothing, et cetera, 6 months in advance? I order for the next season." The first problem, of course, for the landlord is, "When can I go out and look for a replacement tenant because, especially if it is an anchor store, I must have someone in that location?"

So, the first of the problems is, "How long until I even know whether that same debtor is going to assume the lease or reject it or, in the other case, assign it?"

DISTINCTION BETWEEN ALLOWANCE AND ACTUAL PAYMENT OF ADMINISTRATIVE RENT

The second problem that you referred to, Senator Heflin, was the time until you get paid. While the code would appear to contem-

plate that when a debtor stays in the premises or even is not in the premises but inhibits the re-leasing of the premises—the code would seem to contemplate that there will be payment as a cost of administration for that time period. But all the code requires is that that payment be allowed.

We have seen some notorious cases where a payment of an administration expense is allowed, but is not, in fact, paid for years. In the *Penn Fruit* case in Philadelphia, costs of administration, which amounted in the aggregate to about $4 million, were not paid—I hope my numbers were right, but the relative numbers are correct—were not paid for close to 5 years. And a fund of some $10 million sat bearing interest during that 5-year period, all to the benefit of the inferior creditors, general creditors, and the administration creditors, the landlord falling in that category, were not paid. So, there are two different time problems: One to payment; another to a decision.

Senator HEFLIN. Did your landlord creditors receive interest on their money?

Mr. FEINSTEIN. No, sir, and there is a Supreme Court case that holds against the payment of interest to creditors in bankruptcy proceedings. I would love to have a large enough interest case where we test that on the administration category creditors. But the answer, Senator, was no, absolutely not.

Now, using those as a prism, I would like to speak to the first two changes that I think this set of proposed amendments would bring about. The first is a change to section 365(d)(1), which would require that the debtor make a decision on whether he will assume or reject the lease within 60 days of a filing of a petition; otherwise, the lease will be deemed rejected. He may, of course, come in and ask for an extension of time, but that shifts the burden of proof upon him to come in and ask for an extension of time.

MINIMUM OF 6 MONTHS BEFORE DEBTOR IS REQUIRED TO ASSUME OR REJECT LEASE

You asked before about statistics. I can tell you that it is certainly a rare contested case where one can get a determination in a chapter 11 of an assumption or rejection of lease within 6 months, and 9 months to 1 year is normative. The delays are built into the code.

You have a filing. It usually takes several weeks before the notices and the number of the case are out. Then there is usually a determination of who can negotiate for the estate. Then a period of negotiation where you try to find out if you are going to stay or not stay.

Then the landlord has his first opportunity to file an application asking for an order to require the debtor or trustee to assume or reject. Usually, the debtor has at least 20 days to respond to that application. Then, in a busy court, it will take 20 to 40 days for that matter to be set down for a hearing.

Then, even assuming an immediate ruling—and those are not so common—but assuming an immediate ruling, the ruling of the judge at that time is, "You, debtor, now have 45, 60 or 90 days"—I

think 60 days is about normative—"to make a decision on whether you assume or reject."

After that period runs, usually on the last day there is a decision, "I will assume or I will reject." It is not operative at that time; that still must go back to the bankruptcy court for approval of the decision to assume or reject. If any party in interest wishes a hearing, again that is a scheduling matter.

Then, even assuming the rejection is effective and the court says, "OK, I approve the rejection," the rejection is not tantamount to vacation of the premises. You can have a lease that has been rejected, but the debtor——

Senator HEFLIN. Go ahead. I am listening and talking at the same time; I am one of those rare individuals.

Mr. FEINSTEIN. The debtor may stay in the premises for 30 to 60 days while he is holding a sale of the fixtures or goods that are on the premises, and only then is the property actually available, and only then can you really effectively go out and look for a replacement tenant.

So, the code itself in its present form builds in an extensive delay in a contested matter of generally 6 months or more.

Section 365(d)(1), the proposed amendments, would apply the same rule we now have in chapter 7 cases to the chapter 11 cases and say that, within 60 days, you must make a decision to assume or reject.

DEBTOR REQUIRED TO PERFORM LEASE PENDING DETERMINATION—TO ASSUME OR REJECT

The proposed amendments to 365(a) would require that while the debtor is in possession, while he keeps the property from being released, while he is waiting to make his decision, he must continue to perform his obligations as a tenant under the lease. We know of a variety of circumstances where that applies.

Remember, first it is not only money that a tenant must perform. Often, a hotly negotiated provision is the covenant to remain open. You have already had testimony about how critical it is to a shopping center when the anchor store or a major store closes. The worst scenario that many of us find our clients in is when a major store closes, and there is a refusal to tell you whether "I will assume or reject," until you go through the whole process that I described before. At the same time, someone is whispering in the client's ear, "Now, if you really want to get rid of this delay, you will pay us so many dollars and maybe we will go away." That is being utilized more and more as a technique in chapter proceedings.

What the amendments to 365(a) would require is that if you have got an obligation under your lease to stay open from 9 to 5 each day, you must do it. If you have got an obligation to provide snow clearing in front of your premises, you must do it. If you have an obligation to pay while you keep that premises out of the marketplace, you have got to do it. That is all the proposed amendments to 365(a) would be doing.

ASSIGNEE TO BE OF FINANCIAL STANDING SIMILAR TO ORIGINAL TENANT

There are two other amendments that I will speak to very briefly, and I think Mr. Cherkis will speak to the others. The proposed amendment to 365(b)(3)(A) and the amendment to 365(d)(2) are both designed to require that a substitute assignee tenant—someone to whom the debtor has sold the lease—that that substitute tenant be of the same financial standing and be held to the same kinds of financial obligations that the original tenant was. It is really, in my view, a clarification of what I think Congress meant in enacting 365(b)(3)(A) originally, where it said you must provide, if you are going to have an assignment, adequate assurance that the assignee will make the payments as you had contemplated before.

Chapter 11 is one of the few places—I cannot think of any other instance in the law, offhand, although there may be some—where businessmen may find themselves required to henceforth do business for terms like 10 and 20 years with someone they never knew before, never contemplated before. A party is coming into the premises solely because he was willing to pay at an auction in a bankruptcy court for the right to come in. That is a long-term arrangement and, at a minimum, it does all sorts of hazard to what we normally think of as freedom of contract and freedom of choice.

But the amendment to 365(d), particularly, and (b)(3), would require that at least when there is such an assignment, the assignee be the same kind of person that the former debtor was at the time he entered into the lease.

Senator HEFLIN. All right, sir; go ahead.

Mr. CHERKIS. Thank you, Senator. I am Laurence D. Cherkis and I am appearing on behalf of the International Council of Shopping Centers.

I am going to focus on section 365(b)(3) of the Bankruptcy Code, which sets forth certain standards for adequate assurance of future performance in the case of an assumption and an assignment of a shopping center lease.

The first aspect of the proposed amendment would provide that in the event of an assignment of a shopping center lease, that assignee is bound by the provisions of that lease, including clauses relating to use, radius and location. We believe that the case law as presently in effect does provide that on an assignment of a lease, the assignee is bound by the provisions of that lease. However, it may be argued that there is an ambiguity in 365(b)(3) which we think was not intended, and we believe the proposed amendment would simply confirm what substantially all practitioners I have ever spoken with believe to be the law; that is, that the assignee of the debtor-tenant, if you will, must be bound by the use clause and the other clauses in the lease that is being assigned.

You have heard the other gentlemen on the first panel this morning speak about the importance of tenant mix and of use. Absent the enforceability of the use clause, or if we were to say that the bankruptcy court had the authority to modify the use clause, substantial problems would be created with respect to tenant use and tenant mix.

The next two amendments in the same section, 365(b)(3), relate to subparagraphs (C) and (D). These sections presently provide that a lease assignment cannot result in a breach of a radius, location or use clause in another lease in the shopping center or in a financing agreement relating to that shopping center—presumably, the mortgage for the shopping center—or a master operating agreement.

Section 365(b)(3)(D) states that the assumption or assignment will not disrupt substantially any tenant mix or balance in the center. The proposed amendment would remove the word "substantially" as a qualification to permitting breaches, if you will, of other agreements in the shopping center, cnd would remove the word "substantially" as a qualification with respect to the preservation of tenant mix.

We believe that inclusion of the word "substantially" in the present legislation creates latitude on the part of the courts to determine what the tenant mix will be and whether an existing radius or exclusive or use clause in another agreement can be breached.

Given the difficulty and sensitivity of the problems involved in balancing out the interests of the various tenants in a shopping center, we submit that the proposed bill would protect existing tenants in shopping centers and their landlords in preserving the structure which they so carefully built in the first place.

The fourth amendment that I am going to address provides that a trustee or a debtor cannot assume a lease which has already expired under State law. This, we feel, confirms existing law; however, certain courts, in their zeal to protect debtors' estates, may interpose their own interpretation of whether or not a lease has been terminated. The amendment makes clear that State law will govern the resolution of this issue.

Finally, we propose an amendment to the automatic stay provisions of the Bankruptcy Code to the effect that there will not be automatically stayed a State court proceeding to evict a tenant under a lease which has already expired. There of course may be some concern that this could create so-called parallel proceedings in the bankruptcy courts and the State courts. What would happen, however, is that if a debtor felt it needed to stay in possession of a store for a reasonable period of time to liquidate its inventory or to find a new place to go, the debtor would apply to the bankruptcy court for a stay of the State court proceedings. If the debtor could justify issuance of the stay, I believe that the stay would be granted on a limited time basis. Once the debtor's need for the location had ceased, the State court proceedings could continue.

I think that, between myself and Mr. Feinstein, summarizes the changes that we have proposed.

Senator HEFLIN. Let me ask you this. Does the Bankruptcy Code now provide basically for any immediate relief and action pertaining to spoilage-prone retail merchandising companies and businesses? Are there certain provisions that require immediate action on the part of the bankruptcy courts on spoilage-prone types of businesses?

Mr. CHERKIS. There has always been in the bankruptcy law an obligation of the debtor or the trustee to marshal and protect and properly liquidate the assets of the estate. In the case of rapidly deteriorating inventory, the debtor would come into court on an expe-

dited basis and ask for authority to sell that inventory out of the ordinary course of business.

I have never seen an instance in which that has been denied. It is often done on oral notice to the creditors' committee—possibly, the secured creditors—and they, certainly, as well as anyone else, want to see that inventory properly protected. So, those orders are given.

Senator HEFLIN. Well, while spoilage-prone inventory is generally considered to have bacterial effects, you have got a similar situation here, while not bacterial in its cause and effect. But do you think your language ought to be directed, say, into the marshaling of assets, or is it, you feel, sufficient as you have got it drawn?

Mr. CHERKIS. I think it is sufficient as we have it here.

Senator HEFLIN. Let me ask you this. Are there problems of antitrust involved in this that ought to be approached as remedial?

Mr. CHERKIS. I do not see the connection, Senator. It is a question of the relationship between the landlord, the tenant, and the other tenants in the shopping centers, which traditionally has been governed in the bankruptcy laws.

Senator HEFLIN. All right. Thank you.

[The prepared statements and other submissions of Messrs. Feinstein and Cherkis follow:]

Prepared Statement of Nathan B. Feinstein

Personal

I am partner in charge of the Bankruptcy and Creditors' Rights Section of the Philadelphia law firm of Cohen, Shapiro, Polisher, Shiekman & Cohen. My firm represents a middle range of entrepreneurs and corporations, and substantial real estate development and financing interests. I have spent most of the last twenty-five years representing borrowers and lenders, offerrors of securities and their purchasers, landlords and tenants, and, more recently, debtors and creditors - hopefully not both at the same time. Although I am appearing before your SubCommittee on behalf of the International Council of Shopping Centers, I hope to bring a broad perspective to these hearings.

I am generally familiar with the presentation of Larry Cherkis, Esquire, to the subcommittee, and will endeavor not to cover the same ground.

General Effect of Amendments

The Proposed Amendments would require the tenant who is a Chapter 11 debtor to adhere as closely as is reasonable to the expectations of the parties who relied upon their lease agreements. If the trustee or Chapter 11 debtor intends to keep the leasing relationship in force, the amendments would require the tenant to perform the rental and other obligations under the lease. If the trustee or Chapter 11 debtor has not made up his mind whether to assume or reject the lease at the time he files his Chapter 11 Petition, the Amendments would require him to make that decision within 60 days. If the lease has terminated or if the trustee has determined to reject the lease, the amendments would require the Chapter 11 debtor to vacate the premises promptly. If the trustee or Chapter 11 debtor opts to sell or assign the lease to a new tenant, the Amendments would emphasize that the new tenant-assignee must be

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of similar financial standing and must undertake the same lease obligations as the original tenant.

The Shopping Center Perspective

I would be a mistake to view a shopping center solely as a real estate investment. In a real sense a shopping center is akin to a small town.

You put down a business root in a town if you believe you will fit in, you believe the town will provide security and other necessary services, and you believe the town will flourish, and your business with it. If the major businesses or other institutions that draw people to town shut their doors, the town will die. If the town's financial base shrinks, the security and other communal services will shrink, and with it will shrink the desirability of the town as a place to visit. If the neighbors with whom you are comfortable leave town, you will soon begin to look elsewhere.

Tenants locate in shopping centers based on the complimentary ability of the various stores in the shopping center to draw customers. One looks to the advertising and merchandising techniques of the larger stores ("anchor stores") in choosing a shopping center. One considers carefully the cooperative advertising, the center promotions, and the parking and other common services performed by the center. The shopping center and its tenants' association rely on a continuing stream of payments from tenant-shopkeepers to meet the snow removal, air conditioning, heating, parking lot maintenance, advertising, mortgage, tax and other obligations of the center. When the stream of payments is disrupted for a significant period of time, every shopowner suffers by the lack of maintenance and uncertain financial viability of the center. When an anchor store closes its doors and stops its advertisements, the smaller tenants suffer the lack of patronage. When Saks Fifth Avenue moves out as anchor store and John's Bargain moves in, the small independent fashion

boutiques die. When the future of the center is in doubt, a businessman-tenant does not know how to order for the next season.

Proposed Amendments to §362(a) and 362(d)(1) [Line 10 on Page 1, and Lines 1 through 5 on Page 2; Lines 1 and lines 6 through 12 on Page 5][1/]
Prompt Assumption or Rejection of Leases

The Proposed Amendment to Section 362(a) [Line 10 on pg. 1, and Lines 1 through 5 on pg. 2 thereof] and the Amendment to Section 362(d)(1) [Line 1 on pg. 5 and Lines 6 through 12 on pg. 5] restore a balance between the operating shopping center's needs for performance of a tenant's obligations while he remains a tenant and for a relatively prompt determination of whether the shopping center will have a tenant or a vacancy with which to cope, and the Chapter 11 debtor's need for time to make a decision.

In its present form, Section 365(a) of the Bankruptcy Code permits a Chapter 11 debtor to assume or reject an unexpired lease, but without a prescribed time limitation. Although current Section 365(d)(2) contemplates that a landlord may ask a court to order assumption or rejection in a reorganization proceeding "within a specified period of time", a Chapter 11 debtor is rarely required to make or give effect to that election earlier than six months after the bankruptcy petition has been filed. After receiving notice of the Chapter 11 petition (often several weeks after its filing), the landlord must prepare and file an application with the bankruptcy court, usually allow 20 days or so for a responsive pleading to be filed, at which point the matter is set for hearing (often 20 or 30 days after the responsive pleading in crowded jurisdictions). It is only then that the bankruptcy court will usually "order the trustee to determine within a specified period of time whether to assume or reject such contract or lease". It is a rare case for a bankruptcy court

1/ The bracketed references are to the lines and pages in the Printers Proof of S. 2297.

to direct that the decision be made earlier than 60 days following the issuance of its order. If the landlord's Application is contested and argued, the bankruptcy court may keep the matter under consideration pending an opinion or decision for weeks or months before the order to assume or reject is issued. If the Chapter 11 debtor ("the trustee") then determines to reject the lease, the rejection decision must go back to the bankruptcy court for the court's approval (Section 365(a) specifically requires that the trustee's determination to either assume or reject a lease is "subject to the court's approval", thus requiring additional court action, and a hearing if requested by "any party in interest", before the trustee's election to assume or reject becomes effective). Even then, a court-approved rejection is not tantamount to the tenant's vacation of the premises. Bankruptcy court's have regularly allowed a Chapter 11 debtor who has rejected a lease to remain in the premises for the month or two following the effective date of the rejection to allow time for the debtor to advertise a bankruptcy sale of the goods or fixtures on the premises. In many jurisdictions there is yet an additional delay until a report of the bankruptcy sale has been delivered to the bankruptcy court and court approval secured. I repeat, it is a rare case where an actual vacation of the premises can be secured within six months of the filing of a Chapter 11 petition, and longer delays are common.

The Proposed Amendment would change the introductory clause of Section 365(d)(1) of the current Bankruptcy Code to require that the debtor make a decision respecting the assumption or rejection of executory contracts within 60 days after the proceedings have been initiated. Currently that requirement exists only "in a case under Chapter 7". The Proposed Amendment would make the requirement applicable "in all cases under this title". The requirement to make a decision within 60 days would not be absolute. A trustee or

debtor in possession may ask the court for "such additional time as the court, for cause, within such 60-day period, fixes". If the trustee does not act to assume or ask for additional time during the 60 day period, then the lease is deemed rejected. That puts the shopping center in a position to begin seeking a replacement tenant within a reasonable time after the Chapter 11 debtor has elected to seek the protection of the bankruptcy court.

The addition of the clause dealing with vacation [Lines 6 and 7 on pg. 5] is designed to require a vacation of the premises promptly after rejection. (It must be remembered that securing a court order at any time involves the filing of an Application, and probably a hearing if the trustee or another party in interest demands).

The two sentences beginning on Line 7 of pg. 5 of the printer's bill and running through Line 12 thereof are designed to conform with the proposed amendment to Section 362(a). The first sentence would require that if the trustee remains in the premises for any significant period of time following his election to reject and an order that he vacate the premises, the trustee will at least be required to pay the rentals contemplated under the lease and to perform the other lease obligations during the time (after rejection) that he remains in possession. The second sentence of that proposed amendment to Section 365(d)(1) merely provides that the landlord's acceptance of rental payments or other lease performance following a rejection of the lease and order of vacation will not be deemed an acquiesence by the landlord to the continuation of the lease. There have been a number of bankruptcy court decisions in the past (and there are similar decisions in some states) that acceptance by a landlord of a rental payment after the lease has otherwise been terminated or violated may constitute a waiver of the termination. This sentence merely assures that acceptance of the payments

required to be made under the Proposed Amendments to Section 365(a) and this Section 365(d)(1) will not take away what the amendments are designed to provide.

The Amendment to Section 365(a) [Line 10 on pg. 1 and Lines 1 through 5 on pg. 2] would require the timely performance of tenant obligations under an unexpired lease between the time the Chapter 11 case has commenced and the date of assumption or rejection.

As described above, it is a rare case today in which assumption or rejection of a lease is required in a Chapter 11 case earlier than six months or so after the case begins. Even upon the adoption of the proposed amendment to Section 365(d)(1), it is apparent that 90 days or more will be entailed before a vacation of the premises is effected, and the bankruptcy courts may upon an application by the debtor in possession allow substantial additional times to run. The Proposed Amendment simply requires that the Chapter 11 debtor "timely perform" its obligations during that period.

Most shopping center leases require tenants to pay their share of common area maintenance (security, snow removal, heating or air conditioning an enclosed mall), taxes, rents, and the like. It is obvious that if the tenant opts to remain in possession of the premises, he should at least promptly pay the current lease obligations. The shopping center itself cannot refuse to pay taxes or mortgage obligations, the tenants association cannot refuse to remove snow or provide security, and there is no valid reason that the Chapter 11 debtor who elects to remain in the premises should not perform like obligations.

The matter becomes far more crucial when the Chapter 11 debtor is an "anchor store". Many of the major Chapter 11 cases in recent years have involved anchor stores. Food Fair, W. T. Grant and City Stores may be cited as examples. Those anchor stores had been looked to as primary draws of clientele

to the entire shopping center. The smaller tenants in the shopping center had generally determined to locate in that center based upon the nature of the anchor store. It is apparent that the dry cleaning establishment located next to a food supermarket depends on the continued operation of the food market to draw customers. A shoe store or fashion boutique depends upon the advertising and continued operation of the Saks or Marshall Fields department store (or some prompt substitute) for its continued viability. In recognition of the importance of the anchor store, the operators of such locations have long been able to negotiate far more favorable terms for their tenancy than have the smaller tenants. That is a simple economic recognition of the importance of the anchor store. In many instances the anchor store undertakes to perform specific services such as snow removal or lighting a major area of the shopping center in exchange for rental concessions in the lease. A hotly negotiated clause in almost any lease is the so-called "operations clause", generally requiring a tenant to remain open during the usual business hours at a shopping center. This is a simple recognition of the communal relationship in many or most shopping centers.

When an anchor store closes its doors or fails to perform its other obligations under a shopping center lease, it causes disaster to the other tenants in the shopping center, to say nothing of the shopping center operator. That condition is exacerbated when the anchor tenant refuses to vacate the premises, or even refuses to indicate its future intention to assume or reject the lease. The small solvent business tenant is then faced with the problem of not knowing what it should order as inventory for the ensuing seasonal periods because it is unable to assess the drawing power of the shopping center during the next several months; indeed, if the snow is not going to be removed or if the lack of anchor store payments will result in an inability of the tenants' association to pay

for other services at the shopping center, the effect can be readily calculated. The Proposed Amendments would simply require that if a Chapter 11 debtor elects to remain in the premises, he shall continue to perform the lease obligations promptly.

The last clause in the Proposed Amendment to Section 365(a) [line 5, page 2], cross-referring to Section 503 of the Code, merely serves to emphasize the ineffectiveness of the current Bankruptcy Code "remedy" designed to insure the meeting of "administrative expense" obligations. Section 503 incorporates the delay problem of requiring an attorney to file an application and attend a hearing before one can even secure an order for payment of an administrative expense, like post-petition rent. Nothing in Section 503 requires the payment of administrative expenses prior to confirmation (and indeed consummation) of a Chapter 11 Plan. That may and often does involve a delay of years, even where it is clear that the estate has and will have sufficient assets to pay for costs of administration. Furthermore, a number of courts have held that no interest is payable by the bankruptcy estate which delays in the payment of those expenses. In at least one notorious case, costs of administration were not paid for five years, while the estate invested almost $10,000,000 at interest rates close to 20% per annum, thus effectively creating a multi-million dollar fund for the payment of inferior creditor claims by the simple device of utilizing funds due for administration payments for the benefit of non-administration class creditors.

Proposed Amendments to Section 368(b)(3) and Section 365(d)(2). [Lines 9 through 11 and lines 15 through 18 on page 3; lines 13 through 17 on page 5.]. Lease Assignments

The Proposed Amendment to Section 365(b)(3) and the Proposed Amendment to Section 365(d)(2) focus on the problem of a lease assignment by the Chapter 11 debtor. It should be remembered that these Sections do not come into play where a

lease itself permits unfettered assignment by the tenant, or where the proposed assignment is agreeable to the shopping center landlord. This comes into play, therefore, only where the lease itself specifically prohibits the assignment, or conditions the assignment to the landlord's consent, and the landlord opposes the assignment. In the original enactment of Section 365(b)(3) of the Bankruptcy Code, Congress evidenced its comprehension that shopping center mix and financial continuity posed unique problems. Notwithstanding the broad "adequate assurance" provisions designed by Congress, many lawyers have experienced a constant narrowing of that intention by bankruptcy courts. These provisions are designed to make the Congressional intent clear, and to amplify that intent based on recent experiences.

The Proposed Amendment to Section 365(b)(3)(A) [lines 9 through 11 on page 3] indicates that when Congress was insisting on the adequate assurance of the post-assignment rent stream, it meant assurances similar to those contemplated by the original parties to the lease when they entered into the lease. There have been those who have expressed the view that the "adequate assurance" to which the landlord was entitled is simply replacement by a tenant of a financial standing similar to the original tenant immediately preceding the filing of the bankruptcy petition-an insolvent for an insolvent! The proposed amendment would make clear that if there is to be an assignment contrary to the landlord's will and contrary to the lease provisions, it must at least be to an assignee similar to the original tenant. If the original had a "triple A credit rating," the substituted tenant should have a similar rating. If the original tenant was an under-funded subsidiary corporation, but whose obligation was guaranteed by a highly rated parent, the proposed assignee should meet a similar standard.

Mortgage instruments covering shopping centers regularly provide that the tenants meet certain financial standards, and particularly that the anchor stores be of high standing. Often it is an event of default for the landlord to allow a tenancy which does not meet those standards. Unless the lease assignee is of a financial standing similar to the original tenant, the landlord runs the risk of having a mortgage default imposed upon him by the assignment.

A greater problem, of course, is the effect on the value of the shopping center. The ability of a shopping center owner to resell the shopping center is almost always directly proportionate to the solidity and financial standing of the shopping center tenants. A shopping center with "triple A" anchor stores and a relatively solid rent stream would normally have a high value. If one substitutes an anchor tenant of inferior financial standing, the resale value of the shopping center (or its ability to re-finance) drops dramatically. That amounts to a clear taking of part of the value of the investor's interest in the shopping center without compensation.

The proposed amendment to subparagraph (c) of Section 362(b)(3) [lines 15 through 18 on page 3] similarly carry forward what isbelieved to be the intention of Congress in the enacting the current Bankruptcy code provision.

As a technical matter, the proposed re-wording makes clear that the assumption or assignment will require compliance with the provisions of the assigned lease, as well as with similar provisions contained in other shopping center leases and agreements. It is possible to read the current language of Section 365(b)(3)(c) as requiring compliance with other leases and instruments, but not necessarily with the lease being assigned.

Of greater significance is the deletion of the "breach substantially" language of the current code provision.

The most significant of the provisions dealt with in

subsection (c) are the "use or exclusivity" provisions. They are almost always carefully drawn and extensively negotiated. More important, they are relied upon by other tenants in the shopping center. If the use provision provides for use by a french restaurant serving haute cuisine, the lease almost certainly intended what it said and others have relied on that assurance. The italian restaurant next store, or the ice cream parlor serving french ice cream is hardly mollified when the bankruptcy court permits the lease to be assigned to an assignee intending the latter uses. That danger exists even though the Bankruptcy Court finds that use by an assignee italian restaurant or a french ice cream parlor would not "substantially breach" the lease between the landlord and the french restaurant tenant who has now become a Chapter 11 debtor and wishes (over the landlord's objection) to assign his lease.

A more important illustration involves assignment of the lease of an anchor store. Consider a shopping center such as the Watertower Shopping Center in Chicago, Illinois, which has as its anchor stores a Marshall Fields Department Store and a Lord & Taylor Department Store. The character of that shopping center is established by those stores as a "high end" shopping center, attractive to smaller boutiques, relatively expensive men's clothing stores, fashion shoe stores and similar uses. Depending on the character of the anchor stores, the other tenants have entered into long term leases. Consider what happens if one or both of those anchor stores file Chapter 11 proceedings, and the leases are assigned to John's Bargain Basement and J.C. Penney or Sears. This is not to suggest that the latter are not fine department store tenants. It is to make clear that they are department stores with a dramatically different appeal than Lord & Taylor or Marshall Fields. The proposed amendment is designed to eliminate the ability of the Bankruptcy Court - which may have an interest in increasing the resale values of leases "for the benefit of creditors" - from

varying the agreed restrictions on use or exclusivity freely negotiated by the original landlord and tenant.

Proposed Amendments to Sections 365(c)(3) and 362 (b). [Lines 23 and 24 on page 4; lines 18 through 23 on page 5]. The Terminated Lease Problem

The Proposed Amendments to Section 365(c)(3) [Lines 23 and 24 of pg. 4] and the Proposed Amendment to Section 362(b) [Lines 18 through 23 on pg. 5] deal with the terminated lease problem.

Where a lease has terminated prior to bankruptcy (either because the 10 or 20 year term has expired or because there has been a breach and timely notice of termination), or where after the filing of a Chapter 11 petition the lease has terminated"by virtue of its own terms without regard to the bankruptcy proceedings" (say, because the 10 year term expired a month after the Chapter 11 petition was filed) the business man's expectation is that the landlord-tenant relationship is at an end. This has proven not to be the case.[2/] Courts (or trustees) have interpreted the stay provisions of Section 362(a) of the Bankruptcy Code as inhibiting the landlord from taking immediate possession of the premises even after expiration of the lease, provided possession of the premises was not transferred prior to the filing of the bankruptcy petition.

The Proposed Amendments are simply an attempt to make clear that a lease which expires after bankruptcy by the lease terms itself, or terminates prior to bankruptcy by whatever action or lease terms are appropriate under state law, is indeed terminated.

Consider this example. Many long term leases provide for some extension or renewal option if the option is exercised three months or six months prior to the expiration of the ten or twenty year term. When that option date passes without exercise, the landlord begins immediately to seek a replacement

2/ See, for Example In re A.L.S., Inc., 1 CBC 2d 516

tenant on the assumption that the premises will be available at the end of the lease term. Indeed, where there is an active and successful shopping center, the landlord will generally have entered into a lease contract with the replacement tenant prior to the actual termination of the earlier lease (but after option or renewal exercise date) so that there will be no vacancy in the shopping center. The tenant is happy to enter into such a lease even though the premises are not immediately available, because he can order his goods and fixtures and other operating requirements long in advance for delivery on his expected occupancy date. If the tenant under the expired lease can by virtue of filing a Chapter 11 petition hold up the delivery of occupancy, he thwarts the expectations of the parties, without having any real legal or equitable interest in the premises, other than the staying power given him by a bankruptcy court or the Bankruptcy Code. It is respectfully submitted that Congress never intended this result. These two amendments would make clear than when a lease has come to an end prior to bankruptcy or by its own terms, the lease is indeed at an end.

Conclusion

Judicial enforcement of agreements is the heart of a free enterprise system. Our society is characterized by businessmen agreeing to buy and sell, to borrow and repay, to lease and occupy; agreements reached by hard bargaining. It is the free determination of "from whom will I buy and what price", and "to whom will I sell under what terms" that undergirds what we call Freedom of Contract. "No...Law impairing the Obligation of Contracts" emerges early in any study of the American judicial, political or economic system.

Chapter 11 turns all of that on its head. A businessman finds that his source of supply has suddenly ceased. A shopping center tenant who entered into a long term lease relying on the May Company Department Store or Food Fair

Super-Market advertising to draw customers to the shopping center, finds that reliance misplaced. The shopping center tenants' association that counted on monthly payments from the members of the association to pay for security, snow removal, parking lot maintenance and other critical services finds that it must suddenly cut back on those required functions. A landlord who undertook financial obligations based upon solemnized leases finds that his income stream has partly terminated and that he is unable to meet his tax and mortgage commitments. Were it not for Article I Section 8 of the Constitution, almost all would concur that much of the Bankruptcy Code was unconstitutional (and parts may well be).

The Proposed Amendments would require a shopping center business tenant which invokes the protection of Chapter 11 to act promptly so that its contractual relationship with the other businesses and with the mutually dependent obligations of the shopping center may be clarified.

The debtor usually has the opportunity to carefully plan invocation of a Chapter 11 proceeding. Rarely does a financial crisis occur overnight. The debtor, better than all the world, knows of his growing financial stringency. The words "we'll file a petition" emerge early in negotiations after a bank sends a "demand letter" or a landlord institutes action to collect unpaid rentals. Such litigation or negotiations are always conducted in the shadow of a Chapter 11 filing. The common experience among lawyers is that a Chapter 11 petition is generally filed after negotiations have broken down or is filed between the time a state court has entered a judgment and eviction or other execution on the judgment has occurred. To the well-counseled business-man in financial difficulties, Chapter 11 is merely one of the alternative tools for dealing with his difficulty. At the time a well-counseled Chapter 11 is filed, the debtor has some idea of the potential source of the funds which will be utilized to effect his

Chapter 11 proceeding. For example, the principal shareholders or their friends will have agreed to advance funds to implement the reorganization provided the debts of the business can be scaled down. Unless there is an availability of funding, or assets which can be sold to produce funds, or a similar basis for infusing capital, a Chapter 11 proceeding is little more than a prelude to the ensuing Chapter 7 liquidation: a prelude during which the debtor's officers, favored suppliers, legal and financial advisors, and occasionally secured parties (particularly where the secured loans have been personally guaranteed by officers or shareholders) will be paid for current services.

This is not to be critical of either Chapter 11 or of those debtors who seek to utilize that available tool. It is simply to suggest that Chapter 11 is a legally available tool, and should be viewed in the context of one of the debtor's available tools to oppose the creditor's or landlord's legally available litigation, judgment execution, and debt foreclosure tools.

The point is that tenants and landlords have legitimate expectations regarding their mutual lease obligations. This mutuality becomes crucial in a multiple tenant shopping center. The Proposed Amendments are designed to limit the adverse impact of a Chapter 11 filing on the solvent tenants in a shopping center.

Prepared Statement of Laurence D. Cherkis

I am a member of the New York City law firm of Wachtell, Lipton, Rosen & Katz and have been engaged in the practice of real estate and creditors' rights law since 1970. I have negotiated and written numerous shopping center leases, have handled many sales and financing transactions involving shopping centers, and have participated extensively in a substantial number of insolvency cases, including W.T. Grant Company, Hartfield-Zody's, Inc., National Bellas Hess, Inc., United Merchants and Manufacturers, Inc. and Food Fair, Inc. I am the author of the chapter on executory contracts and leases appearing in 4 Collier, Bankruptcy Practice Guide (Matthew Bender 1981). I am appearing before your Subcommittee on behalf of the International Council of Shopping Centers. The views expressed herein are my own and do not necessarily reflect the views of my firm.

This memorandum discusses the provisions of the Bill (1) amending Section 365(a) of the Bankruptcy Code to provide that the obligations of a debtor-tenant under a lease are to be performed on a current basis after the entry of the order for relief under the Bankruptcy Code, (2) amending Section 365(d)(1) to provide for a 60-day period for assumption or rejection of leases in all cases under the Bankruptcy Code, (3) amending Sections 365(b)(3)(A) and 365(d)(2) to provide that the financial standing of a proposed assignee of a shopping center lease be similar to that of the original tenant as of the date the lease was executed and providing for security deposits from such assignees in certain instances, (4) amending Section 365(b)(3) to confirm that the Bankruptcy Court may not authorize the assignment of a lease by a debtor-tenant if the proposed

assignee will breach any of the lease terms, including radius, location, use and exclusivity clauses, (5) eliminating the word "substantially" from Sections 365(b) (3)(C) and (D) of the Bankruptcy Code, and (6) amending Section 362(b) to provide in substance that the automatic stay will not apply to state court eviction proceedings against a debtor which fails to vacate premises after its lease has expired.

Current Payment of Use and Occupation Charges; Assumption and Rejection of Leases Within 60-Day Period

The Bill would amend Section 365(a) of the Bankruptcy Code to provide that the obligations of a debtor-tenant under a lease are to be performed on a current basis from and after the date of the order for relief under the Bankruptcy Code. The Bill would further amend Section 365(d)(1) to provide that in all cases (not just chapter 7 cases) a lease must be assumed or rejected within sixty days after the order for relief, or within such additional time as the court, for cause, within such sixty day period, may establish. If the lease is not assumed or rejected within such sixty day period, it is deemed rejected.

These two amendments are designed to remedy a number of abuses.

First, under current law, a debtor-tenant is obligated to pay use and occupation charges (and not rent) under a real estate lease until the lease is assumed or rejected. The payments are to be based upon the fair value of the benefit conferred upon the estate for the use of the premises. American Anthracite & Bituminous Coal Corp. v. Leonardo Arrivabene, S.A., 280 F.2d 119, 124-126(2nd. Cir. 1960); 120 Wall Associates v. Schilling, 266 F.2d, 548, 550

(2d Cir. 1959), affirming In re North Atlantic and Gulf S.S. Co., 166 F. Supp. 29 (S.D.N.Y. 1958). Thus, the use and occupation payments made by the debtor the landlord may be in an amount less than the rent reserved in the lease. The landlord in these circumstances may be compelled to make up any shortfall required to pay debt service, taxes and operating costs of the property, and is therefore compelled in substance to finance a portion of the debtor's insolvency case until the lease is assumed or rejected. The proposed amendment to Section 365(a) would eliminate this problem.*

If the debtor has vacated the premises prior to the assumption or rejection of the lease, no payments for use and occupation will be required inasmuch as the estate is not receiving any benefit from the premises under current principles of law. See 120 Wall Associates v. Schilling, supra. In the case of a shopping center property, a debtor may vacate the premises, leave the store unoccupied, and not pay any charges therefor until the lease is assumed or rejected. Moreover, the debtor may defer assumption or rejection of the lease until it can effectuate a sale of that lease pursuant to Section 365(f) of the Bankruptcy Code. In most cases, the proceeds of sale will be paid to

* Although under present law use and occupation payments are to be made on a current basis (even if in an amount less than the rent reserved in the lease), the payments are not always timely made. This creates an even greater burden on landlords, who may be constrained to apply to the court repeatedly in order to compel payment. In a case filed in the Southern District of New York, In re The Valley Fair Corporation, Case No. 77-B-2978, the debtor was the lessee of three large discount department stores located in New Jersey. The debtor remained in possession of these premises for the months of April through November 1978 without paying use and occupation charges. In addition, the debtor failed to pay the real estate taxes payable under the leases. With respect to one of the three stores, the landlord was also a tenant under an overlease of the property, so that the failure of the debtor to pay use and occupation charges required the landlord to reach into its own pocket to pay the rent under the prime lease. This was particularly egregious inasmuch as the landlord had itself recently emerged from a Chapter 11 proceeding. The use and occupation payments were not made until a settlement in the case was reached in December, 1978.

the debtor and its general creditors and not to the landlord. Of course, in order to assign a lease, the debtor must first assume the lease under Section 365(b) of the Bankruptcy Code and cure all past defaults. However, in the interim period, the debtor has again compelled the landlord to finance the debtor's lease assignment program.

If the debtor's lease assignment program is successful, and the lease is ultimately assumed and assigned, the debtor and its creditors will have benefited from the landlord's inability to collect use and occupation charges. The landlord, on the other hand, will merely have been restored to its original position. If, however, the lease is not assumed and assigned, and is instead rejected, the landlord will be relegated to a general unsecured claim for damages arising from the rejection of the lease (Bankruptcy Code §365(g)), but will have no claim for post-petition use and occupation charges inasmuch as the premises were not being occuppied by the debtor.* Hence the debtor will have obtained a free ride from the date of the order for relief until the lease is rejected. The proposed amendment to Section 365(a) would provide current compensation to the landlord while the debtor determines whether or not it will be able to assign its lease.

The rules governing the payment of use and occupation charges arose through case law developed under the former Bankruptcy Act. See 3A Collier on Bankruptcy, ¶62.14[2] (14th Ed. 1975). Under Section 70b of the Act, clauses in leases providing for termination were enforce-

* Furthermore, the landlord's claim for damages arising out of the lease rejection is limited in amount in accordance with a formula set forth in Section 502(b)(7) of the Bankruptcy Code. The only other type of claim limited in a similar manner is that of an employee under a rejected employment agreement. Bankruptcy Code §502(b)(8). Lessors under equipment leases and non-debtor parties to contracts and mortgagees are not so limited.

able.* Therefore, landlords were able generally to avoid assignments of their leases by debtor-tenants by terminating the leases, so that the question of the debtor's liability for use and occupation payments for a vacant store pending assumption and assignment of the lease was not of significance. Under the Bankruptcy Code, however, bankruptcy default clauses in leases are not enforceable and the leases are assignable. Bankruptcy Code §§365(b), (e) and (f). It is therefore appropriate to reconsider, as the Bill does, the effect of the old rules relating to use and occupation charges in the light of the Bankruptcy Code's policy of fostering lease assignments by debtor-tenants.

The proposed amendment to Section 365(d)(1) provides that the trustee or debtor must assume or reject a lease within sixty days after the order for relief, or within such additional time as the court, for cause, within such sixty day period, may establish. The purpose of this amendment is to provide landlords of chapter 11 debtors with some measure of certainty as to the disposition of their property and to limit the time in which a store may remain vacant while the debtor determines whether to assume (and perhaps assign) or reject the lease. The effect of a vacant store, and especially a vacant anchor store, upon a shopping center and the other tenants therein is obvious. There may be a substantial loss of traffic, an image of decline, and difficulty in recapturing customers who have turned to competing facilities.

The proposed amendment shifts to the debtor the burden of justifying an extension of the sixty day period,

* The courts, in an effort to avoid forfeitures, engrafted a number of doctrines onto Section 70b to preserve the leases where the only material default was the commencement of the bankruptcy proceeding itself. See, e.g. Speare v. Consolidated Assets Corp., 360 F.2d 882 (2d Cir. 1966); Queens Boulevard Wine & Liquor Corp. v. Blum, 503 F.2d 202 (2d Cir. 1974).

rather than compelling landlords to incur the expense, delay and uncertainty of litigation in moving the court under Bankruptcy Code §365(d)(2) for an order compelling the debtor to assume or reject a lease within a period determined by the court. There are several examples of cases under the former Bankruptcy Act in which landlords have elected to waive all or a part of their claims against the debtor in exchange for a lease rejection instead of incurring such expense, delay and uncertainty. Thus in the W.T. Grant Company case (United States District Court for the Southern District of New York, Case No. 75-B-1735), the debtor had embarked upon a program to contract its operations, thereby necessitating the vacation of many of its locations. However, in many instances Grant would surrender possession of store premises but failed to apply to the Court for authority to reject or assume the lease of the premises. In return for a prompt rejection of a lease, Grant offered and received from a number of landlords agreements waiving a part or all of the landlords' post-petition administrative claims and pre-petition claims together with claims arising out of the rejection of the lease.

A purported class action was filed against Grant as debtor-in-possession alleging that the agreements with the landlords had been unlawfully obtained. Berger and Lee v. W.T. Grant Company, Debtor. Although the case was ultimately dismissed, and Grant's actions were found to have been permitted under the Bankruptcy Act, it exemplifies the feeling of many shopping center owners that they should be entitled to an expeditious assumption or rejection of their leases as a matter of law.

Substantially the same practice was followed in a case entitled In re Hartfield-Zody's, Inc., Case No. 74-B-

1633, which was also filed under the old Bankruptcy Act in the United States District Court for the Southern District of New York. Harfield-Zody's was a retailer having locations in Michigan and California. During the 1974 recession, the Michigan locations, which were substantially dependent upon the welfare of the automobile industry, became highly unprofitable and Hartfield-Zody's was forced to divest itself of such locations. Hartfield-Zody's accordingly entered into numerous agreements with landlords of the Michigan properties (and indeed certain landlords of its unprofitable California properties), which provided for claim waivers substantialy similar to the waivers described with respect to W.T. Grant Company above.

Similarly, in the matter entitled In re The Walter Reade Organization, Inc., Case No. 77-B-42 (filed under the old Bankruptcy Act in the Southern Distict of New York in January 1977), certain landlords of Walter Reade motion picture theaters likewise executed agreements waiving certain claims in exchange for a prompt rejection of their leases.

The proposed amendment to Section 365(d) may, therefore, reduce the period within which store properties remain vacant, enhance landlords' ability to obtain an expeditious determination as to the disposition of leases in reorganization proceedings and enhance landlords' bargaining power in negotiations relating to the waiver of their claims.

Financial Standing of Assignees; Security Deposits

The Bill also proposes an amendment to Section 365(b)(3)(A) of the Bankruptcy Code providing in substance that an assignee of a lease should have financial standing similar to that of the original tenant under the lease as of

the date the lease was executed. Under Section 365(f) of the Code, "adequate assurance of future performance" must be provided in connection with the assignment of a lease. The amendment seeks to limit the discretion granted to the courts under the Bankruptcy Code to determine whether adequate assurance of future performance has been provided by establishing minimum standards for the financial wherewithal of proposed assignees. Similarly, the proposed amendment to Section 365(d)(2), providing for security deposits in certain cases, likewise adds substance to the concept of adequate assurance of future performance.

Binding Effect of Use Clauses and Other Lease Terms Upon Prospective Assignees

The Bill proposes an amendment to Section 365(b)(3) to provide in effect that the Bankruptcy Court may not authorize assignment of a shopping center lease if the assignee will breach any of the terms of the lease, including terms relating to radius, location, use and exclusivity. This amendment resolves what may be an ambiguity in Section 365(b)(3)(C) as to whether the Bankruptcy Court has the power to change a use clause in a shopping center lease in order to foster an assignment of the lease to a different type of user.

The use clause in a shopping center lease is of major importance to a shopping center landlord and to the other tenants in the shopping center. Annexed to this submission as Exhibit A is the transcript of a seminar held under the aegis of the International Council of Shopping Centers in 1978 relating to "tenant mix" for small shopping centers. The participants in the seminar discuss the considerations involved in blending different types of anchor tenants in a center, the effects of discount stores,

supermarkets, fast food operations and motion picture theatres, the proper location of these facilities, and their effects on parking layouts and pedestrian traffic flow. It is readily apparent from the transcript that the tenant mix in a shopping center lease is a matter of sophisticated real estate expertise which may affect the viability of an entire center or of certain tenants therein. It is likewise clear that a change of use of an anchor store in a shopping center may have a materially adverse effect upon the satellite tenants. The proposed amendment to Section 365(b)(3) would confirm that an assignee of a shopping center lease will be bound by the terms of the lease, including any restrictions on use contained therein.*

Elimination of the "Substantiality" Standard

The Bill also proposes an amendment which will eliminate the word "substantially" from Section 365(b)(3)(C) and (D). Inclusion of the word "substantially" in these provisions permits the courts to authorize lease assignments which to the degree determined by the court may violate an existing radius, location, use or exclusivity clause in another lease or agreement. Elimination from these provisions of the word "substantially" will not, however, diminish the courts' power to interpret such clauses or to authorize the assignment of a lease to a party which will comply with the limitations contained therein. As demonstrated above, compliance with the operational structure created and maintained by a shopping center landlord may be critical to the viability of the center.

* Annexed hereto as Exhibit B is an April 20, 1982 decision of the United States Bankruptcy Court for the Southern District of New York (In The Matter of U.L. Radio Corp., Bankruptcy No. 81 B 11067), authorizing the assignment of a lease by a debtor engaged in electronics sales to a restaurant operator despite a clause in the lease limiting the use of the premises to electronics sales. The case did not involve a shopping center.

The proposed amendment merely seeks to confirm that the courts will enforce these arrangements.

Inapplicability of the Automatic Stay to Certain State Court Holdover Proceedings

The Bill also proposes an amendment to Section 362(b) of the Bankruptcy Code to provide in substance that the automatic stay will not apply to state court eviction proceedings against a debtor which fails to vacate premises after its lease has expired. This amendment will require a debtor who desires to retain possession of the premises to apply to the Bankruptcy Court for an order enjoining the state court proceedings. If, for example, the debtor can demonstrate that it needs the premises to liquidate its inventory, or to continue its business while it finds a new location, the Bankruptcy Court may issue the injunction (See Bankruptcy Code §105(a)). If the injunction is not issued, the Bankruptcy Court will have found that possession of the subject premises is not required for reorganization or liquidation.

Under the former Bankruptcy Act and the Bankruptcy Rules, the automatic stay was substantially narrower in scope than the automatic stay set forth in Section 362(a) of the Bankruptcy Code. It was therefore standard practice for debtors' attorneys to obtain at the outset of a case a broad judicial stay if the need therefor could be demonstrated to the court. The proposed amendment, in reviving this practice in a narrow context, merely shifts to the debtor the burden of justifying its retention of the space in lieu of compelling the landlord to initiate proceedings to obtain relief from the automatic stay so that it may recapture property with respect to which the debtor's lease has expired. Thank you for the opportunity to appear in this matter.

EXHIBIT A

Shopping Center Report
AN EXCLUSIVE SERVICE FOR MEMBERS OF ICSC

INTERNATIONAL COUNCIL OF SHOPPING CENTERS / 665 FIFTH AVENUE, NEW YORK, N.Y. 10022

Tenant Mix for Small Centers

Developers and retailers discuss tenant mix considerations in small shopping centers

PANELISTS:

Chairman: Richard C. Biagi,
Vice president for real estate, Lucky Stores, Inc., Dublin, Calif., a diversified retail company, which operates more than 1250 supermarkets and other retail stores throughout the U.S. Former vice president and trustee of ICSC.

Richard D. Bronson,
President, R. D. Bronson Companies, Bloomfield, Conn., a shopping center development company which has developed large and small projects from New England to Tennessee. Former ICSC state director.

Albert B. Glickman,
Senior partner, Glickman, Crumpler, Riley & Associates, Beverly Hills, Calif., developers of some 150 shopping centers, principally community and neighborhood projects. Former trustee, ICSC.

Norman B. Krons,
Senior vice president, Physical Resources, Walgreen Co., Chicago, operators of more than 640 Walgreen drugstores and over 300 food service units. Trustee, ICSC.

E. W. (Ed) Spieckerman,
Vice president, real estate, Radio Shack, a division of the Tandy Corporation, Fort Worth, operators of more than 4,000 Radio Shack stores throughout the U.S. and Canada.

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Growing in numbers as well as sophistication, small shopping centers now are facing many of the same kinds of tenant mix questions that have been applicable to regional projects.

Tenant mix for small centers was the subject of a wide-ranging discussion at ICSC's annual convention in May, 1978.

The following is an edited transcript of the panel discussion among developers and retailers active in the small center field.

It covers, among other points, which new tenant types are entering small centers, what developers and retailers think about small center mix, preference in store location and co-tenancies, and what developers can do to improve their mix.

BIAGI: I'd like to ask the developers—from their observations—to tell us what new types of tenants are beginning to show up in small centers. What trends do they see as far as the neighborhood and community type shopping centers are concerned?

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GLICKMAN: I find that there is a dramatic change. Not more than five years ago the biggest problem in building small centers was overbuilding of satellite stores. From our experience we found that a heavy ratio of satellite space may have looked good on paper and in our pro formas but when completed the space was very difficult, if not impossible, to lease.

However, the pendulum swings, and things do change. Several years ago we said that if you built a market and a drug store, plus some free-standing buildings like banks and savings and loan associations, you shouldn't put in more than 10,000 to 15,000 square feet of satellite stores.

We are now finding that we build 50 per cent to 100 per cent more satellite space and lease it. Several centers that we recently built in the 200,000-square-foot-range have as much as 60,000 square feet of satellite space, including restaurants, financial institutions and free-standing buildings. The same generally applies to smaller centers with supermarkets and drug stores. Secondly, home improvement centers are now playing a big role in small centers. Another big space user is the catalogue store. As for some of the smaller tenants, amusement centers, fast food shops, health spas, weight clinics and now discos are considered viable small-center tenants.

But the most significant thing is the return of the soft goods tenants . . . the fabric, shoe, dress and men's stores. They have been gone from small centers for 10 or 12 years, but they are coming back and they are very successful in our centers. It could well be that the reason for their return to smaller centers is the relative high cost of going into regional centers. It stands to reason that the more traffic you have in the center, the better these tenants will perform.

These tenants are finding that they need to do only 50 per cent to 60 per cent of sales volume as compared with regional centers to make the *same profit* due to lower occupancy costs.

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BRONSON: In smaller centers, particularly those in New England, we haven't seen any exciting new tenant types . . . mostly convenience stores, discount health and beauty aids, and the like. Chains have become a bigger factor in recent years in small centers. They are aggressively looking for locations. The small convenience food stores also are cropping up quite often.

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BIAGI: What you said at the end is significant; the cost of mall space per square foot is forcing some of the soft goods tenants back.

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GLICKMAN: It is more than just pure rental costs. Usually in regional centers, the developer gives tenants a shell and it costs them so much money to put their stores in.

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BIAGI: In other words, it is the economics of being involved in a regional center that is pushing this trend. I'd like to amplify that just a bit. From my own observations, it looks as though some of these highly specialized tenants—the specialty dress stores and, more recently, shoe stores—are particularly interested in smaller centers that are in the immediate vicinity of a regional center. You will find those types of tenants attracted to the site because of the traffic drawn by the regional. In this way they get the automobile exposure to the storefronts without paying the tariff of mall rents.

How about our two retailer panelists? Do you have anything to add on the new types of retailers that you see in small centers?

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KRONE: One of the things we are seeing is the growth of specialty grocery stores. By that I mean the store that sells produce only, or meats only; the limited line type of operator. In some cases they may sell high end merchandise; in others they can be described as discounters. One of these is known as Aldi. We had an operation in one of our Globe stores in Houston called Agmar that is a high-end produce operator tied in with a produce wholesaler. In the Chicago area we are seeing a number of the former National and A & P stores taken over by both Aldi and Agmar type operations. In some cases I expect to see them in the same building, but divided up under two different managements.

They have proven to be good traffic builders for us and very desirable co-tenants. We are taking a harder look at locating next to an Aldi-type operator than we would have in the past. Our stores, as an example, have a great deal of general merchandise; these operators do not. Therefore, in the same development with the same amount of traffic, we are able to capture the general merchandise or drugstore type merchandise business that formerly was going in part to the 40,000 square foot supermarket sitting next to us.

The discotheque, on the other hand, I think is a negative merchandiser within the center and we are looking into its effect on us.

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BIAGI: On discos, you indicated that you are checking them very carefully. I, as a neighborhood retail tenant, would be very much concerned about the kind of traffic they would attract. However, discos are becoming

more an accepted type of entertainment and they do not necessarily cater to one type of clientele.

The problem with discos, comes in terms of the hours they operate and the physical arrangement of the center.

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SPIECKERMAN: I have to agree that discos are probably an undesirable tenant for other retail operations. I say that not just because of the clientele they attract and the empty beer bottles, etc., but because they take up a lot of parking space that could otherwise be used for retail merchants.

One of the most significant trends that was brought out earlier is the return of the specialty store. You cannot even call it a return, because many are locating for the first time in strip centers. They are doing this mostly for economic reasons . . . high rents, high cost of building stores in regional malls. But I think a lot of them are now looking to neighborhood market penetration to a greater degree than they did in the past.

Another very significant development has been the grocery store. Not so many years ago, a grocery store was 18,000 to 20,000 square feet. Essentially it was a food store, although it carried a few cosmetics. Today, you are finding supermarkets in the 40,000 plus square-foot range with a wide selection of merchandise, hard goods and soft goods. Many of them are becoming departmentalized. They may carry wide selections of delicatessen specialty foods, plants, hardware and so on.

It is really amazing. I think this is good for the center and other tenants. It's a traffic builder. Their appearance has improved. Their design is so much more attractive than it used to be.

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BIAGI: Actually, if one were to analyze what a small center is, the first characteristic that comes out would be the limited amount of retailing space available. Since specialty-type retailers concentrate a greater depth of a particular line of merchandise in a small space, it makes them a natural for a small center.

I think you will find that those who pick off a segment of retailing and become specialists in it, (i.e. a strata of the shoe business or a segment of the dress business, or the limited-type grocery that we were talking about) are natural tenants for a well-located small center. If some of you have not seen the Aldi stores in the Midwest that we talked about earlier, they are only about 4,000 square feet and they carry something like 850 items of staple grocery products.

Supermarket operators are not necessarily happy about that, but it's a development that is coming along and must be recognized.

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QUESTION FROM FLOOR: I'm working on a development that is not really downtown, but in an area two or three miles away. I was wondering what the tenants on the panel look for when considering a location close to downtown, that is totally built up residentially, but is going through a tremendous revitalization.

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KRONE: We are looking, as are most drug chains, for exactly that kind of location. For example, within the city of Chicago, we hope to develop about 25 in-city stores in the next three years.

They represent to us an identifiable market that suburban areas do not have. The density and concentration allow us to have more stores. We are permitted to develop our units in smaller centers. Neighborhood associations or local councilmen will see to it that municipal parking is provided or paid for so that parking is not included in common area maintenance. This saving enables us to be more effective in keeping up the security of the store.

There are real economic benefits and the trade-off obviously is the higher rent paid for the land cost. But we are excited about in-city locations and I think everybody in our industry is.

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SPIECKERMAN: I have to second what has been said. We believe in city locations and we're now developing a downtown project of our own in Fort Worth, Texas. We are not developers, but it will include our home office, a couple of other office buildings, a hotel and ice skating rink, and about 200,000 square feet of retail space.

I am encouraged by what is going on in the inner areas of many of our large cities. I would like to see U.S. cities have the same vigor that we see north of the border in Canada, like in Montreal and Toronto.

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BRONSON: I am pleased to hear the tenants speaking that way. Today, developers are faced with a rather unique situation. One, almost all tenants are looking for new locations. They are looking for more stores and are very expansion minded. Money is readily available. Notwithstanding the fact that rates are moving up, money is still there for the right project for the right developers.

So you have got tenants looking for locations and money available for the developer. But the problem today is getting what we call the right to build. The problems range from conservation, preservation, curb cuts, air quality, and the like.

We are finding a lot less resistance when we go to develop in-city locations. We find the towns and the local citizens encouraging, not going out of their way to try to organize the bird-and-bunny groups that often come out of the woodwork to stop major centers.

As a developer, I am very pleased to hear the tenants speak so favorably about in-city locations. Such loca-

tions are becoming more and more of a factor in terms of our new projects.

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QUESTION FROM FLOOR: This is directed to Mr. Glickman. How do you lease 60,000 square feet of satellite stores when your major anchor has restrictions in its lease which prohibits discos, cocktail lounges, movie theaters, amusement centers, convenience markets and a whole list of others?

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GLICKMAN: In the first place, when I spoke of as much as 60,000 feet, I was referring to a center that is usually around 200,000 to 240,000 square feet total, a 20 to 25 acre center.

But when a store like Lucky Stores says, for example, that it doesn't want a theater in the parking lot, they usually don't mind if it is far away from them. Sometimes you can even negotiate that the theater be located 400 or 500 feet away.

As to the whole question of exclusives, with the threat of the FTC and other factors, most tenants are now limiting their restrictions. In fact, we are finding fewer and fewer requests for exclusives and restrictions.

Everything is negotiable and certainly a theater must be considered part of the tenant mix, no matter where it is located on the site. When you lay out your shopping center the theater can be put in the corner of the parking lot. First you must figure the theater's parking needs, then place the structures where there is sufficient parking to support it and still not interfere with store needs.

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BIAGI: The concern most supermarkets have is the tremendous turnover of parking spaces involved in supermarket shopping. The same situation probably applies for super drug stores.

In the case of supermarkets, we are dealing with a large percentage of women shoppers, who require a large band of available, convenient, close-up parking. In California and much of the West, women shoppers don't use the package pick-up service nearly as much as they do in the Midwest and the East. And, believe it or not, shoppers actually wheel shopping carts with their own groceries out to their car faster than most pick-up arrangements. In addition, wage scales are such that we cannot afford to have convenience or courtesy people around to provide the service. As a result, usurping close-in parking is harmful to the supermarket operator. This not only applies to movie theaters, but to health spas, gymnasiums, beauty parlors, various types of schools and so forth. As a result, the developer must recognize the term of the parking that is characteristic of particular types of tenants and place them where they can operate without killing off the retail side of your shopping center.

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QUESTION FROM FLOOR: I would like to ask the entire panel to respond to a question on the destiny of major discount stores in a neighborhood center. Are they a good draw for other tenants?

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SPIECKERMAN: Absolutely. I think a major discount operator is the greatest asset that a neighborhood or community type of center can have. In our operation, for example, we just love to be in a center with K mart or Target; stores that are good, solid discount operators that advertise heavily and draw a lot of traffic.

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KRONE: We are now finding it to be advantageous. However, for a long time, we felt it was a problem because of the overlapping lines of merchandise. One thing we found is that the layout of the center is critical to the success of the convenience stores if there is a large discounter in the center. If the discounter is put up front, and the grocery and drug are placed deep in the site, it will be harmful for most convenience merchants. This holds true even if the discounter is successful. The discounter will draw the people even if they are deep in the site, thus enabling you to give the prominent positions near the road to the grocer and the drugstore. There also is the problem of stability of parking.

A typical drugstore has some 1,700 people visit it daily. We have to turn the parking spaces near the store frequently. As a result, the long-term shoppers who go to a large department store or discount store have to be segregated on the site.

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GLICKMAN: We're doing 14 projects now and 11 of them have discount stores in what I call small centers. That sums up our view on discounters.

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BRONSON: We're bullish on discount stores, particularly in New England. We find that the so-called anchorless shopping centers just don't come off too well. They may work very nicely in the Sun Belt states and in places that are densely populated. But in New England, we find that most tenants basically live off one major draw, and without a major you have problems. As a result, we are anxious to have discount department stores in our centers when we can get them.

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QUESTION FROM FLOOR: I have more of a comment to make than a question. What's happened in recent years is that the start-up of new regional centers is a very minimal situation. There is a pretty good lead time. It is a lengthy process that really restricts the opportunity for a mall tenant, particularly in fashion soft goods, to move ahead at the rate that it would like to.

Secondly, with the energy crisis, a lot of attention is being directed to closer-in residential units. Many blue collar type areas which were overlooked in the rush ... suburbs are undergoing revitalization.

Thirdly, there is the advent of so many new types of tenants, and some discounters have become quite good. Thus, many enlightened developers are seeking a balanced mix once again in small centers. A lot of developers have recognized the fact that if you have a discounter on one end and a food store on the other end, or a discounter and a relatively weak general department store, you can develop a more unified appeal for the center by developing a fashion mix within the mall itself.

By getting 30 to 50 stores, a lot of developers today are beginning to find that, with proper balancing and upgrading the mix, the center can draw from a wider area and a broader range of customers than if it was primarily discount and service. A lot of good fashion retailers are beginning to take a hard look at these markets, not only because they are cheaper, but because they really afford an opportunity to do a productive job at a fairly high profit ratio. A regional center represents high cost, and it can be very high yield. Smaller centers are relatively low cost, but they can also ...duce very high yield.

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QUESTION FROM FLOOR: Do you think a catalogue-type showroom operation dealing only in hard goods can be a suitable substitute for a discount operation as an anchor tenant, provided that you also had a grocery store and a drugstore? They usually occupy about 60,000 square feet, a portion of which is used for warehousing goods.

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BRONSON: I just made a deal with such an outfit. We find that they are a viable alternative to a typical discounter. They will draw almost as much traffic and they are a suitable operator. In another arrangement in Massachusetts we have this type of tenant in the same center with a major discounter, which is somewhat of a unique departure from the earlier position that they had taken. Because of the scarcity of good new locations, many of the major tenants are softening their stance on who they will and will not go with as co-anchors.

...ICKMAN: We find them very desirable. Catalogue operators usually require that you have a heavy soft goods tenant in the center as co-anchor. A discount store will fill the bill. They are terrific traffic generators and do very well in our centers. As developers of small centers we really court them.

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SPIECKERMAN: From a tenant point of view, I second that. They are excellent anchor tenants. They don't necessarily have to be substitutes for a discounter, but they could be an addition to one.

I would like to comment on one thing that Norm Krone said earlier about the discounter and its placement within the shopping center. I disagree on putting the discounter off to one part of the center, preferably in the back, and putting the grocery and drugstore and the satellite tenants up front. I think the very advantage the discounter offers is the possibility of creating foot traffic. In small centers ordinarily you do not have much foot traffic and by putting the discounter off to one corner of the shopping center you defeat that very purpose. I like to see discounters smack in the middle, provided of course there is enough parking for everybody.

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QUESTION FROM FLOOR: In reference to movie theaters, I would like to know what kind of contribution they make to the mix of tenants. After all, they operate at night when the center is closed. They have no crowds during the day and cannot afford the rent that a retail tenant can pay.

We have twin movie theaters in a mini-mall. We know for a fact that people arrive there at seven o'clock. They line up at the window to buy tickets and, by the time they leave the mall is closed. We can get at least three times the rent from an office building than from a movie theater if we would convert it.

Why then are developers interested in putting movie theaters in their centers?

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BRONSON: I would like to comment on this question, if I may. It is a significant question. The major tenants, like supermarkets, discount and drug stores, are really concerned about parking. We do put theaters in our centers, but they are far enough away. Theaters do push a tough rent deal, but we usually put them in the least desirable part of the parking lot. As to malls, theaters usually just have a little frontage on the mall ... a little entrance, with most in the back.

The important point is we want to generate traffic. If we have some excess land that doesn't hurt anybody and we cannot do anything else with it, I think theaters are a tremendous generator of traffic. They have a great draw. People will drive as many as 5 and 10 miles to a theater where they usually will not drive more than two miles to a supermarket. If we are generating more traffic and more action in our shopping center and not hurting the parking, I think theaters are a terrific generator and I think it falls in the tenant mix.

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QUESTION FROM FLOOR: I would appreciate some comments from the panel, particularly from Mr. Glickman as a shopping center developer and owner, as to the placement of small tenants within a strip center. We are developing strip centers of 150,000 to 200,000

square feet with 50,000 to 60,000 square feet of small tenants. We have been placing our soft goods merchants on one end of it and the hard lines on another end. We are starting to get complaints from the hard line merchants that they are not getting the traffic that the soft lines are pulling. I would appreciate your comments on that. I have a second question directed particularly to Mr. Spieckerman. Given the preference or opportunity of going into a strip center or a mall, both in the same general location, which would be better for your company and why?

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BIAGI: Why don't we take that second question first, Ed.

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SPIECKERMAN: I don't think you're comparing apples and apples. You do not necessarily locate in one to the exclusion of the other. We try to get into all good regional malls in the country and in Canada that we can. But the regional mall draws from a much wider area than the strip shopping center. Quite often, we have had stores in established strip centers and a year or two later a regional mall is being developed across the street or within a very short distance. We have located in the mall as well. But we did not close our strip center store.

A lot of people may feel that the mall is going to kill that little store, but that's just not so. The little store showed healthy sales increases and the mall store, of course, got off to a quick start and did a big volume right from the beginning. But it takes a lot more volume to support a mall store than it does to support a strip center store.

The great majority of our customers are men. The guy who wants to buy an antenna on Saturday afternoon, or some parts and pieces, is in his old overalls or shorts and doesn't want to go into a mall. He would much rather drive right up to the store, pick up what he needs and go on about his business.

So really, we are talking about two different things. There is a great need for strip center locations and the vast majority of our stores, about 87 or 88 per cent, are in strip centers, neighborhood centers or free-standers. Only about 12 per cent are in regional malls.

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BIAGI: Al Glickman, will you respond to the layout question?

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GLICKMAN: Your question raises a very significant problem. Sometimes the site dictates the solution. But if you are going to have 40,000 to 60,000 square feet of satellite space, you must give those people the prime location.

Now, a supermarket, drugstore or discount store will take between 150 and 200 feet of depth and on your plot plan it would be ideal to put them all in one bank and then put all those small stores over to the side wherever they fit. I've done this and it is pure suicide.

All you do is keep changing those small tenants. If you are going to merchandise that much satellite space, you must give them what I call 100 per cent location and you'd better put your anchors on the end. This encourages foot traffic and helps the smaller satellite tenants to survive.

Taking all big, deep stores and lining them all up in a row is bad. You must give the smaller tenants the 100 per cent location. They are a developer's bread and butter. They pay the highest rents. If there is a constant turnover because they are going out of business, this creates real problems for the success of a center.

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BIAGI: Well, in essence, what we are looking at is a compromise of forces, the physical constraints, the shape of your property, the press of your major tenants to want to be at certain locations, and the need to have your satellites situated in between those major tenants so that you can maximize the exposure and foot traffic.

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QUESTION FROM FLOOR: There has been an increasing number of national specialty chains showing an interest in strip centers or mini-malls. Some developers feel the national specialty chains have the name recognition, the merchandising power, and the advertising power, and they must be attracted for a successful strip center or mini-mall. How do you feel about strong locals as opposed to national chain specialty stores?

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BRONSON: I think it is very important to have local operators, and they are just as important as the rated tenants. Many times, lenders jam tenant mix down our throats. In many instances they have a pre-lease requirement specifying the number of rated tenants to have in a particular center. And even though you may feel that a particular local tenant would be a good draw for your center, you are not able to make the deal with them up front because the lender is demanding Triple A rated tenants. So, to a degree, the lender dictates the tenant mix in a shopping center.

Local operators are obviously a big plus. You have to have a good mix of not just fashion and convenience stores, but also a good mix of national tenants as well as local operators.

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QUESTION FROM FLOOR: A few years ago we saw a sprinkling of some enclosed sidewalk type centers. Most agree that a grocery store and probably a drugstore don't belong in an enclosed sidewalk. But since we are reaching for more soft goods type tenants, I wonder what the reaction would be to enclosing the sidewalk for a portion of the center as a way to improve the tenant mix, with the thought of drawing some more soft goods type tenants into the center.

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BIAGI: I can start off with a reaction to that. The enclosed sidewalk or climate-controlled sidewalk is directly related to the climatic conditions that are involved. In a number of areas it could be just a waste money. In certain areas it is a real must. I can see it in the Northeast and I can see it in some of the very hot humid areas. Usually enclosed sidewalks feed into the front corner of the superdrug at, say, one end and the supermarket at the other end, so that they really form both extremes of the enclosed sidewalk. Your other specialty tenants are sprinkled in between. It is an ideal shopping environment, but you must weigh the need for it against the economics involved in actually constructing and maintaining the center. More than ever, utilities and power costs are an extremely important factor. So it takes very careful consideration.

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KRONE: From a purely economic standpoint, I would say you can do it if you want. But we are not going to tie into it and we are not dependent on it. Therefore, make sure those people who front on it pay all the costs . . . maintenance, heating and cooling.

In the locations where we are tied into enclosed sidewalks, I don't think they have contributed to our sales and I am not yet convinced they contribute to the sales of the small tenants. We have one center that we actually developed, but no longer own, that had an enclosed sidewalk. The current owner got rid of the enclosure and was able to save $15,000 of his own money in maintenance, heating and cooling—costs he would not have been able to pass to the entire strip.

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SPIECKERMAN: I agree. If a tenant does not want to tie into an enclosed sidewalk and if he does not want to share in the cost of running it, well, what good is it? I was quite excited a few years back when they started building a few in Houston. They were nice looking centers, very well done, but the tenants inside the enclosed sidewalk got very little traffic. Everybody did exactly what they do in an open sidewalk center . . . they pulled up in front of the grocery store and in front of the drugstore. They'd get their shopping done and get back into their cars and drive off. The smaller tenants on the inside did not do well at all.

Another great disadvantage is that of identification. One thing I look for in a neighborhood location is good sign exposure. That is very important to us. Our sign is internationally known and we advertise heavily. We would like to have our sign as big as possible—out there for everybody to see. If you are inside an enclosed sidewalk shopping center, your signing possibilities are severely limited. For that reason I urge developers even in the humid climates to spend their money somewhere else; you would probably get a much better return.

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BIAGI: What it really boils down to is you have got to be very careful. It is a great idea when you have tremendous foot traffic, and you see that in the larger malls. The tendency of people shopping for convenience products is to go to a particular major tenant, get their merchandise and then leave.

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QUESTION FROM FLOOR: My question is directed towards the desirability of fast food or take-out food tenants. Are they desirable in terms of others retailers? If so, to what percentage of the mix? Lastly, should they be banked together or distributed throughout the center?

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BRONSON: Lately we have noticed that McDonalds is taking some in-line locations. Friendly Ice Cream was a forerunner of in-line locations. Of course, the developer looks at the pad location with a somewhat slanted view. Economically, it is a tremendous rent payer and a plus for the center. It may even be possible for a developer with a few pad locations to secure enough rent from those locations to pay for the entire piece of property that he is developing.

Fast food places are terrific traffic generators. They are excellent tenants. If you can get them to go in-line I think you are helping the other merchants in the center as much as you are helping your own development. Typically, the fast food tenants are credit or rated tenants. This can be a big plus insofar as the lender's desire to have as much rated income as possible in the center.

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SPIECKERMAN: From a retailer point of view I wholeheartedly agree. If you can get the likes of McDonalds to locate in-line by all means do it. The only problem is parking. They do take up a lot of parking spaces and if you don't have adequate parking, then you hurt your fast food tenant and the other merchants.

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KRONE: Our position is that they are very desirable. My experience with McDonalds, Burger King and others now going into the strips is that even when they are in-line they are not really taking interior locations. They are really taking an anchor position at one end nearest the highway location. It closely approximates pad-type positioning. By so doing they also solve a parking problem because you have end space which would otherwise be unusable for the other tenants. They generate traffic, give tremendous exposure to the rest of us in the center. If you have a quality operator, we are in favor of it.

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GLICKMAN: Since we are now building more satellite space in small centers, I would say up to 20 to

25 per cent could be devoted to food. Not all of it should be the McDonalds-type operations. I would say that on 60,000 square feet of satellite space, at least 15,000 square feet of the in-line space could be made up of chicken places, ethnic food—small operators who are traffic generators and are anxious to get into the shopping center.

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BIAGI: I'm going to ask one final question of both the retailers and developers on the panel. As far as the retailers are concerned, what have developers been doing wrong in small convenience type neighborhood centers?

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SPIECKERMAN: I think that the basic problem has been a lack of professionalism in the past. I am greatly encouraged to see that more professionals are getting into strip center development than ever before. Some of the major mall developers now have strip center divisions and are applying the lessons they have learned in building malls to the strip center business. I think this is excellent.

But what went wrong in the past is that many people thought that they could just go out and develop a shopping center. Many of them had money, bought a piece of property somewhere, built a shopping center without any regard to the neighborhood, or of the desirability or the need for the center. These projects became nothing more than useless eyesores. The tenant mix quite often is bad because the only thing they looked for was rent dollars. They don't have the first idea of what tenant mix is. They would just as soon put in a dentist or real estate office as a retail tenant.

The other thing is the appearance of the center, its construction. Many of them were cheaply constructed and show it. There is no sign uniformity and no sign restrictions resulting in a hodge-podge of cheap signs. The parking area quite often is insufficient. It is not well maintained. The lighting is inadequate. Ingress and egress are bad. These are problems directly attributable to the lack of knowledge on the part of the person or the individuals who developed the center and a money lender who did not know much more than the guy he loaned the money to.

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KRONE: I think lack of professionalism is probably the key thing. Site planning in many small centers is deplorable and I would strongly suggest that the major tenants be heard. The long-term investment in small centers is made by two, three or four principal tenants and the developer should listen to their advice. They are interested not only in trying to help themselves, but the entire center. Over the 15, 20, or 25 years that they intend to rent, they want to ensure the viability, success and continued profitability of every tenant in the center. In this way, it is not going to be solely a selfish interest, but rather for the good of all tenants trying to operate in that particular development. The problem is that many developers will not take the advice of the major tenant.

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BIAGI: I think it is a point well made. Speaking as a retailer, the fact is that retailers do not have a monopoly on brains; it is just that we've done it so many times that we have had a chance to make more mistakes than anybody else. Experience is nothing more than the opportunity of having made a lot of mistakes and hopefully learning by them. Developers could benefit from our experience and mistakes.

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QUESTION FROM FLOOR: I would like a comment on the feasibility of a merchants association in a small strip center.

■

BIAGI: A merchants association for a small center makes little sense to me. It is just too formal, too powerful for the base over which it is going to be spread, and you are going to hear this from every major retailer. They spend thousands of dollars a week promoting their chain and your center along with it. You don't have a big enough budget in a center of 15 or more acres to support a professional, highly trained promotional director. As a result, promotion will be the stepchild of some store manager or developer who will take care of it in his spare time. The whole thing is completely out of whack economically and practically speaking.

It is a great idea in a larger center where you have the money base, the number of tenants and the size of contribution to do a job. In my view, the question of promotion in a small center should be relegated to a couple of seasonal things throughout the year. You simply do not have the economic base to support someone to do the job properly.

■

SPIECKERMAN: You are 100 per cent right. I do not join merchants associations in the small centers because they are like the United Nations . . . you have all the little nations that do not have any money who do all the talking and then vote on how to spend your money. I just don't believe in that.

■

EXHIBIT B

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In the Matter of	:	Bankruptcy No. 91 B 11067
U.L. RADIO CORP.,	:	
Debtor.	:	MEMORANDUM & ORDER

A P P E A R A N C E S:

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New York, New York

FILED
APR [illegible] 1992
JUDGE J. GALGAY
BANKRUPTCY JUDGE

JOHN J. GALGAY - Bankruptcy Judge

Debtor, U.L. Radio Corp., has moved for an order, pursuant to Bankruptcy Code section 365(f), authorizing it to assume its lease ("Lease") with Jemrock Realty Company ("Jemrock"), the landlord, and authorizing U.L. Radio to assign the Lease to Just Heaven Restaurant, Ltd. ("Just Heaven"). U.L. Radio operates the leasehold as a television sales and service store. Just Heaven, the prospective assignee, will operate the premises as a small bistro. Jemrock opposes such an assignment, citing a use clause in the Lease which provides that the lessee shall use the premises only for television service and sale of electrical appliances. Jemrock asserts that the assignment of the Lease to Just Heaven would unlawfully modify the Lease by violating the use clause. Such modification, Jemrock avers, is not permitted under section 365 without the landlord's consent, which consent Jemrock withholds.

After a hearing, the Court ordered the parties to submit proposed findings of fact and conclusions of law [hereinafter "Findings and Conclusions"]. The Court has considered all the papers submitted by the parties, the oral arguments and the applicable law and legislative history. The Court grants debtor's motion to assume and assign the Lease to Just Heaven.

I. Background

On September 17, 1979, the debtor entered into the Lease with Jemrock for a store located at 2656 Broadway, New York, New York. The store is located in a building which is also occupied by a grocery store, a Chinese restaurant, a liquor store, and 170 apartments. The term of the Lease is for ten years. The rent required to be paid is as follows: $9600 per year from November 1, 1979, to October 31, 1982; $10,800 from November 1, 1982,to October 31, 1985; and $12000 from November 1, 1985 to October 31, 1989. Paragraph 43 of the Rider to the Lease provides that the tenant may assign the Lease with the written consent of the Landlord, which consent is not to be unreasonably withheld.

On May 20, 1981, the debtor filed an original petition under Chapter 11 of the Bankruptcy Code and continues to operate its business as debtor in possession. No creditors' committee has been formed. The debtor intends to propose a liquidation plan of reorganization. The debtor is current in the payment of rent and related charges required by the terms of the Lease and is not in default of any of the Lease terms.

In furtherance of its intention to liquidate all of its assets and to propose a plan of reorganization, the debtor, subject to the approval of this Court, entered into an assignment of the Lease to Just Heaven. The proposed assignment provides, inter alia, that Just Heaven will pay to the Debtor as consideration for the assignment as follows:for the period commencing three months after this Court's approval of the

assignment to October 31, 1988, the sum of $2000 per month. Such payments will fund a plan paying unsecured creditors 100 percent of their claims. Rockwell International, the largest creditor, recommends the assignment.

The president of Just Heaven has executed a personal guarantee for the payment of rent in favor of the landlord for the first two years of the assignment, together with a statement that her net worth exceeds $50,000.

The Lease provides in paragraph 45 of the rider to the Lease that "any noise emanating from said premises shall be deemed a breach of the terms and conditions of this Lease." Just Heaven has allocated $20,000 for construction, including soundproofing. David Humpal St. James, Vice President and Secretary as well as a director and a shareholder of Just Heaven, is a noted interior designer including the design of commercial restaurants. His design work has involved soundproofing. See Affidavit of David Humpal St. James.

II. Issues

Two issues confront this Court:

> (1) Have the provisions of section 365, regarding assumption and assignment of leases, been satisfied?
>
> (2) Can deviation from a use clause prevent the assignment of a lease, when the assumption and assignment otherwise comport with the requirements of section 365?

III. Assumption and Assignment Under Section 365

Code section 365 governs the assumption and assignment of executory contracts, providing broad authority to a trustee or debtor in possession[1] to assume and assign an unexpired lease. 11 U.S.C. §365(a); see Report of the Committee on the Judiciary, Bankruptcy Law Revision, H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 347 (1977) [hereinafter "House Report"];

1/ Footnotes omitted.

Report of the Committee on the Judiciary, Bankruptcy Reform, S. Rep. No. 95-989, 95th Cong., 2d Sess. 58 (1978) [hereinafter "Senate Report"]; In re Lafayette Radio Electronics Corp., 9 BR 993,997 (BC EDNY 1981); 2 Collier on Bankruptcy ¶365.01 (15th ed. 1981). The aim of this statutory authority to assume a lease is to "assist in the debtor's rehabilitation or liquidation." House Report at 348; Senate Report at 59.

Assignment of a lease,which is at issue here, must comply with section 365(f), which states:

> (f)(1) Except as provided in subsection (c) of this section, notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law, that prohibits, restricts, or conditions the assignment of such contract or lease, the trustee may assign such contract or lease under paragraph (2) of this subsection.
>
> (2) The trustee may assign an executory contract or unexpired lease of the debtor only if --
>
> (A) the trustee assumes such contact or lease in accordance with the provisions of this section; and
>
> (B) adequate assurance of future performance by the assignee of such contract or lease is provided, whether or not there has been a default in such contract or lease.
>
> (3) Notwithstanding a provision in an executory contract or unexpired lease of the debtor, or in applicable law that terminates or modifies, or permits a party other than the debtor to terminate or modify, such contract or lease or a right or obligation under such contract or lease on account of an assignment of such contract or lease, such contract, lease right, or obligation may not be terminated or modified under such provision because of the assumption or assignment of such contract or lease by the trustee.

Subsection (f)(1) "partially invalidates restrictions on assignment of contracts or leases by the trustee to a third party." House Report at 349; Senate Report at 59; see Fogel, Executory Contracts and Unexpired Leases in the Bankruptcy Code 64 Minn. L. Rev. 341,360 (1980) [hereinafter "Executory Contracts"]. Subsection (f)(2) "imposes two restrictions on assignment by the trustee: (1) he must first assume the contract or lease, subject to all the restrictions found in the

section; and (2) adequate assurance of future performance must be provided to the other contracting party." House Report at 349; Senate Report at 59.[2] Finally, subsection (f)(3) "invalidates contractual provisions that permit termination or modification in the event of an assignment, as contrary to the policy of this subsection." House Report at 349; Senate Report at 59.

A. Requirements of Assumption

The first requirement of assignment under section 365(f)(2) is proper assumption under section 365. 11 U.S.C. §365(f)(2)(A). The broad authority of a trustee or debtor in possession to assume is limited in Code section 365 by subsections (b), (c), and (d). House Report at 347; Senate Report at 58.

Section 365(b)(1)and (2) prescribe conditions to assumption of a lease if a default has occurred. "Subsection (b) requires the [debtor] to cure any default in the...lease and to provide adequate assurance of future performance ...before he may assume." House Report at 347; Senate Report at 58; 2 Collier on Bankruptcy ¶365.04 (15th ed. 1981). No default exists under the Lease before this Court; therefore, the subsection (b) requirements for assignment are not applicable.

Section 365(c) prohibits a debtor from assuming a lease if applicable nonbankruptcy law "independent of any language in the contract or Lease itself" excuses the other party from giving performance to or receiving performance from someone other than the debtor. House Report at 348; Senate Report at 59.[3] Such "nondelegable" and, therefore, non-assumable contracts and leases include those for unique personal services, as well as those to extend credit, to make loans, and to issue securities. The Lease before this Court does not fall under the prohibition of section 365(c). See In re Taylor Manufacturing, Inc., 6 B.R.370 (N.D. Ga. 1980).

Section 365(d) sets time limits on the assumption of un-

expired leases. The time requirements of subsection (d) have been met and are not at issue.

B. Adequate Assurance of Future Performance

The second requirement of assignment under section 365(f)(2) is adequate assurance of future performance ("adequate assurance"). 11 U.S.C. §365(f)(2)(B). Adequate assurance also appears in section 365(b) as a requirement of assumption if an executory contract is in default. 11 U.S.C. §365(b)(1)(C). The phrase "adequate assurance of future performance" is not found in the Bankruptcy Act.

Adequate assurance is not defined in section 365(f) nor in the legislative history of section 365(f), but "[t]he definition should generally be the same as in section 365(b)." Fogel, Executory Contracts at 362. In the legislative history of section 365(b), Congress while discussing assumption under section 365(b) and the bankruptcy clause under section 365(f), provided this explanation of adequate assurance:

> If a trustee is to assume a contract or lease, the courts will have to insure that the trustee's performance under the contract or lease gives the other contracting party the full benefit of the bargain."

House Report at 348; Senate Report at 59.

Beyond equating adequate assurance with the full benefit of the bargain, Congress offers no definition of adequate assurance except in the case of real property leases in shopping centers.[4] The Lease at issue here is not located in a shopping center. Congress described a shopping center as "often a carefully planned enterprise, and though it consists of numerous individual tenants, the center is planned as a single unit, often subject to a master lease or financing agreement." House Report at 348. The building in which U.L. Radio is located is primarily a residential apartment building, with a liquor store, a grocery store, a restaurant, and U.L. Radio on the first floor. Thus the specific provisions of adequate

assurance in the shopping center case do not apply to the assignment at issue here. See In re Lafayette Radio Electronics, 9 B.R. at 998.

Apart from shopping center leases, Congress "entrusted the courts with the definition of adequate assurance of the performance of contracts and other leases." Fogel, Executory Contracts at 359. Adequate assurance of future performance are not words of art, but are to be given practicial, pragmatic construction. What constitutes "adequate assurance" is to be determined by factual conditions. In re Sapolin Paints, Inc. 5 B.R. 412,420-21 (BC EDNY 1980); In re Lafayette Radio Electronics, 9 B.R. at 998. The broad authorization of the trustee or debtor to assume or assign unexpired leases, notwithstanding anti-assignment or bankruptcy clauses, prompted the admonition from Congress that the courts must "be sensitive to the rights of the nondebtor party to... unexpired leases." House Report at 348; Senate Report at 59.

The phrase "adequate assurance of future performance" was adopted from Uniform Commercial Code section 2-609. Report of the Commission on Bankruptcy Laws of the United States, H.R. Doc. No. 93-137, 93d Cong., 1st Sess. Pt II 156-57 (1973). U.C.C. section 2-609 provides that a party with reasonable grounds for insecurity regarding another party's performance may demand "adequate assurance."[5] Official Comment 4 to section 2-609 discusses, inter alia, Corn Products Refining Co. v. Fasola, 94 N.J.L. 181, 109 A.505 (1920), and James B. Berry's Sons Co. of Illinois v. Monark Gasoline & Oil Co., Inc., 32 F.2d 74 (8th Cir. 1929), and indicates that "adequate assurance" focuses on the financial condition of a contracting party and his ability to meet his financial obligations. Regarding adequate assurance under an assignment pursuant to section 365(f)(2), the Court in In re Lafayette Radio Electronics stated, "[T]he Court's primary focus will be on the ability of [the assignee] to comply

with the financial obligations under the agreement." 9 B.R. at 998.[6]

In In re Pin Oaks Apartments, 6 BCD 1396 (B.C. S.D.Tex. 1980), the Court found that changes in financial provisions of a lease, a percentage rental clause and a sublease provision which protected that rental clause, precluded a finding that adequate assurance had been provided because of the drastic effect the changes would have on rentals received.

Thus, the primary focus of adequate assurance is the assignee's ability to satisfy financial obligations under the lease. In this case, the president of the assignee has executed a personal guarantee of the payment of rent in favor of the landlord for the first two years of the assignment, together with a statement that her net worth exceeds $50,000. The assignee has budgeted $20,000 for construction, enhancing the chances of success of the assignee's enterprise. The assignee will have operating capital of an additional $30,000. Affidavit of David Humpal St. James at p.3. Upon these facts, the Court rules that adequate assurance of future financial performance has been provided by the assignee.

IV. Use Clause

However, adequate assurance of future financial performance is not the complete statutory requirement; adequate assurance of future performance is. The financial capability of an assignee may be sufficient for a finding of adequate assurance under an executory sales contract or a similar commercial transaction. In a landlord-tenant relationship, more than an assignee's ability to comply with the financial provisions of a lease may be required. More particularly, will compliance with a use clause be required in order to provide adequate assurance?

Congress indicates that adequate assurance will give

the landlord the full benefit of his bargain. House Report at 348; Senate Report at 59. In its case-by-case determination of those factors, beyond financial assurance, which constitute the landlord's bargain, the Court will generally consider the provisions of the lease to be assigned. See In re Lafayette Radio Electronics, 9 BR at 998 (a "landlord cannot be granted any greater rights than what the lease provides"); In re Pin Oaks Apartments, 6 BCD at 1400 (citing Hurley v. Atcheson, Topeka & Santa Fe Ry., 213 U.S. 126 (1909), for the proposition that assumption and assignment of a lease entails acceptance by the assignee of the burdens as well as the benefits of the lease).

However, it is equally clear that, by requiring provision of adequate assurance under section 365, i.e., "the lessor's receipt of the 'full benefit of his bargain'," Congress did not require the Court to assure "literal fulfillment by the lessee of each and every term of the bargain." Simpson, Leases and the Bankruptcy Code: The Protean Concept of Adequate Assurance of Future Performance at 35 (unpublished draft in Bankruptcy Court, S.D.N.Y.) [hereinafter "Leases"]. Section 365, by its own terms, empowers the court to render unenforceable bankruptcy clauses and anti-assignment clauses which permit modification or termination of a lease for filing in bankruptcy or assignment of the lease. 11 U.S.C. §365(e),(f)(3). Section 365(k) relieves the estate of liability for future breaches of a lease after assignment, notwithstanding lease provisions to the contrary. 11 U.S.C. §365(k); see Simpson, Leases at 39.

The Court in In re Pin Oaks Apartments argued that court authority to abrogate lease provisions extends only to those provisions expressly stated by Congress:

> If Congress intended to give this Court or the trustee the power to abrogate any contractual rights between a debtor and non-debtor contracting party other

> than anti-assignment and "ipso facto" [i.e. bankruptcy] clauses, it would have expressly done so.

6 BCD at 1398.

Such a narrow view of court authority is not supported by the statute or the legislative history. First, such a narrow view would frustrate the express policy of Congress favoring assignment. Under the Pin Oaks reasoning, lessors could employ very specific use clauses to prevent assignment and thus circumvent the Code. Section 365(f), in broad language, empowers the Court to authorize assignment of an unexpired lease and invalidate any lease provision which would terminate or modify the lease because of the assignment of that lease. 11 U.S.C. §365(f)(1),(3). Any lease provision, not merely one entitled "anti-assignment clause", could be subject to the court's scrutiny regarding its anti-assignment effect. The court could render unenforceable any provision whose sole effect is to restrict assignment, "as contrary to the policy of [subsection (f)(3)]." House Report at 349; Senate Report at 59.

Further, when Congress intended that all terms and provisions of an agreement remain unaltered, it expressly stated such an intent. Section 1124 sets down stringent requirements to define unimpaired claims, requiring the cure of defaults and the unaltered maintenance of legal, equitable,and contractual rights. 11 U.S.C. §1124(2)(D). As one commentator points out, these expressed, stringent requirements for unimpaired claims differ from the requirement that Congress mandated under section 365 - mere provision of adequate assurance. Simpson, Leases at 40-1. Under both sections 1124 and 365, Congress expressly stated the requirements. Under section 365, literal compliance with all lease terms was not required. Even under the tightly drawn definition of adequate assurance in the shopping center case, Congress

did not envision literal compliance with all lease provisions; insubstantial disruptions in, inter alia, tenant mix and insubstantial breaches in other leases or agreements were contemplated and allowed. 11 U.S.C. §365(b)(3)(C),(D); Simpson, Leases at 28; In re Russell Johns, 1 CBC 2d 174 (B.C. D.Nev. 1979) (insubstantial change in use of leasehold located in shopping center, from adult discotheque to male striptease showcase, permitted).

Thus, provision of adequate assurance of future performance does not require an assignee's literal compliance with each and every term of the lease. The court may permit deviations from strict enforcement of any provision including a use clause. See Simpson, Leases at 41.

One commentator suggested that the court render completely invalid any use clause in a non-shopping center lease because: (1) "the lessor is seeking to protect his tenant mix with the lease provision, and the Code does not requir the court to provide such protection"; and (2) a use clause "invalidly conditions assignment." Fogel, Executory Contracts at 364 (footnote omitted); see Simpson, Leases at at 37 n.45. The Court rejects this "per se unenforceable" reading of a use clause.

However, the Court will not go to the other extreme and adopt the "insubstantial" breach or disruption standard for non-shopping center cases that is applicable only to shopping center leases. The insubstantial breaches and disruptions language of section 365(b)(3) "clearly reflects an attempt to limit the effects of what was understood-- and feared-- to be the more expansive authority conferred by the balance of [s]ection 365(a)." Simpson, Leases at 37-38 (referring to Krasnowiecki & Vass, Shopping Centers and the New Bankruptcy Code, 36 Bus. Law. 79,92 (Nov. 1980); see Fogel, Executory Contracts at 359). The Court's authority to waive strict en-

forcement of lease provisions in the non-shopping center cases will permit deviations which would exceed those permitted in the shopping center cases. See Simpson, Leases at 39.

Within the range between unenforceability of a use clause and insubstantial breaches of a use clause, the Code provides no specific standard by which to measure permissible deviations in use. Whatever standard is applied must serve the policy aims of Congress.

Section 365 expresses a clear Congressional policy favoring assumption and assignment. Such a policy will insure that potential valuable assets will not be lost by a debtor who is reorganizing his affairs or liquidating assets for distribution to creditors. This policy parallels case law which disfavors forfeiture. See In re Huntington Limited, 654 F.2d 578,584 n.7 (9th Cir. 1981); 2 Collier on Bankruptcy ¶365.06 n.1 (15th ed. 1981). To prevent an assignment of an unexpired lease by demanding strict enforcement of a use clause, and thereby contradict clear Congressional policy, a landlord or lessor must show that actual and substantial detriment would be incurred by him if the deviation in use was permitted.

In this case, the contemplated deviation in use is from an appliance store to a small bistro. The building in which the unexpired leasehold is located already contains a restaurant, a laundry, and a liquor store. The landlord has failed to demonstrate any actual and substantial detriment which he would incur if the proposed deviation in use is permitted. The Court also notes that the contemplated use, along with the planned soundproofing, will have no adverse effect on other tenants in the building. Thus, this Court rules that the use clause may not be enforced so as to block assignment of this lease to Just Heaven. The

fact that Jemrock withholds its consent to the proposed assignment will not prevent the assignment. Consent is required only in leases governed by section 365(c). The lease here is not subject to section 365(c). See In re Taylor Manufacturing, Inc., 6 BR 370,372 (B.C. N.D. Ga. 1980).

Finally, the Court briefly addresses the constitutional issue raised by the deviation in the contractual terms of the lease. Can a landlord assert a violation of the Fifth Amendment which prohibits the taking of property without due process of law? The Court in In re Sapolin Paints, Inc., 5 B.R. 412 (BC EDNY 1980), denied the enforceability of a bankruptcy clause, stating:

> 'Bankruptcy proceedings constantly modify and affect property rights established by state law.' Wright v. Union Central Life Ins. Co., 304 U.S. 502,517...(1938). The power given Congress by Article I, Section 8, of the Constitution to establish uniform laws relative to bankruptcy gives it broad latitude to effect both contract and property rights. Wright v. Union Central Life Ins. Co., supra; Kriehner v. Irving Trust Co., 299 U.S. 445...(1937); Continental Illinois National Bank & Trust Co. v. Chicago-Rhode Island P.R. Co., 294 U.S. 648...(1935).

Id. at 423; see In re Huntington Limited, 654 F.2d 578, 590 (9th Cir. 1981) (Circuit Court permitted assumption and assignment of a lease and permitted assignee to further hypothecate the lease in contravention of lease provision).

Congress, in section 365, has stated a general policy favoring assignment. Balanced against this general policy as the requirement that the non-debtor contracting party receive the full benefit of his bargain. Jemrock Realty will receive the full benefit of its bargain under the proposed assignment of the leasehold from U.L. Radio to Just Heaven. No defaults exist under the lease. The lease has properly been assumed and Just Heaven has provided ad-

equate assurance of future performance. The landlord has shown no actual or substantial detriment to him from the proposed assignment. The statutory requirements have been satisfied. The assignment is authorized.

It is so ordered.

Dated: New York, New York
April 19th 1982

John J. Galgay
Bankruptcy Judge

Senator HEFLIN. Thank you all. We appreciate your testimony, and a record will be made of this in due course. The subcommittee will endeavor to look closely into this problem.

[Whereupon, at 10:37 a.m., the subcommittee was adjourned.]

PROPOSED LEGISLATION

Calendar No. 764

97TH CONGRESS
2D SESSION

S. 2297

[Report No. 97–527]

To amend title 11, United States Code, to improve the protections for shopping centers and their tenants under the Bankruptcy Code.

IN THE SENATE OF THE UNITED STATES

MARCH 29 (legislative day, FEBRUARY 22), 1982

Mr. HATCH (for himself and Mr. DECONCINI) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

AUGUST 17, 1982

Reported by Mr. THURMOND, with an amendment

[Strike out all after the enacting clause and insert the part printed in italic]

A BILL

To amend title 11, United States Code, to improve the protections for shopping centers and their tenants under the Bankruptcy Code.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

~~That this Act may be cited as the "Shopping Center Protections Improvements Act of 1982".~~

99-782 O—82——9

SEC. 2. Section 365 of title 11, United States Code, is amended to read as follows:

"(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor. The trustee shall timely perform all the obligations of the tenant arising from and after the date of the order for relief, under an unexpired lease (including payment of the rent and other charges specified in such lease) until such lease is assumed or rejected, notwithstanding the provisions of section 503.

"(b)(1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee—

"(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

"(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

"(C) provides adequate assurance of future performance under such contract or lease.

"(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to—

"(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

"(B) the commencement of a case under this title; or

"(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

"(3) For the purposes of paragraph (1) of this section and paragraph (2)(B) of section (f), adequate assurance of future performance of a lease of real property in a shopping center includes adequate assurance—

"(A) of the source of rent and other consideration due under such lease with a financial standing, including guarantors, similar to that of the original tenant when the lease was executed;

"(B) that any percentage rent due under such lease will not decline substantially;

"(C) that assumption or assignment of such lease is subject to all the provisions thereof, including (but not limited to) provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other lease, financing

agreement, or master agreement relating to such shopping center; and

"(D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center.

"(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.

"(c) The trustee may not assume or assign any executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if—

"(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

"(B) such party does not consent to such assumption or assignment; or

"(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor; or

"(3) such contract or lease has been terminated under State law prior to the order for relief.

"(d)(1) In all cases under this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is deemed rejected, and in the case of a lease, the court shall order the premises to be vacated immediately. If the premises are not vacated within 30 days after such order, the trustee shall perform all of the obligations under such lease currently. Acceptance of such performance shall not constitute a waiver or relinquishment of the lessor's rights under the lease or the Bankruptcy Code.

"(2) If an unexpired lease is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.".

SEC. 3. Section 362(b) is amended by adding a new paragraph (9) to read as follows—

~~"(9) under subsection (a) of this section, of a proceeding to obtain possession of property subject to a lease which has expired by virtue of its own terms without regard to the bankruptcy proceedings.".~~

That this Act may be cited as the "Shopping Center Protections Improvements Act of 1982".

SEC. 2. Section 365 (a), (b), (c), and (d) of title 11, United States Code, is amended to read as follows:

"§ 365. Executory contracts and unexpired leases

"(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor. The trustee shall timely perform all the obligations of the tenant, arising from and after the date of the order for relief, upon an unexpired lease (including payment of the rent and other charges specified in such lease) until such lease is assumed or rejected notwithstanding the provisions of section 503 of this title. For cause shown, the court may extend the time for performance of any obligation of rent or other charges due upon an unexpired lease pursuant to the provisions of section 108(b) of this title. Acceptance of such performance shall not constitute a waiver or relinquishment of the lessor's rights under the lease or under this title.

"(b)(1) If there has been a default in an executory contract or unexpired lease of the debtor, the trustee may not assume such contract or lease unless, at the time of assumption of such contract or lease, the trustee—

"(A) cures, or provides adequate assurance that the trustee will promptly cure, such default;

"(B) compensates, or provides adequate assurance that the trustee will promptly compensate, a party other than the debtor to such contract or lease, for any actual pecuniary loss to such party resulting from such default; and

"(C) provides adequate assurance of future performance under such contract or lease.

"(2) Paragraph (1) of this subsection does not apply to a default that is a breach of a provision relating to—

"(A) the insolvency or financial condition of the debtor at any time before the closing of the case;

"(B) the commencement of a case under this title; or

"(C) the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement.

"(3) For the purposes of paragraph (1) of this section and paragraph (2)(B) of section (f), adequate assurance of

future performance of a lease of real property in a shopping center includes adequate assurance—

"(A) of the source of rent and other consideration due under such lease, and in the case of an assignment, with an operating and financial performance, including guarantors, similar to that of the original tenant when the lease was executed;

"(B) that any percentage rent due under such lease will not decline substantially;

"(C) that assumption or assignment of such lease is subject to all the provisions thereof, including provisions such as a radius, location, use, or exclusivity provision, and will not breach any such provision contained in any other lease, financing agreement, or master agreement relating to such shopping center; and

"(D) that assumption or assignment of such lease will not disrupt any tenant mix or balance in such shopping center.

"(4) Notwithstanding any other provision of this section, if there has been a default in an unexpired lease of the debtor, other than a default of a kind specified in paragraph (2) of this subsection, the trustee may not require a lessor to provide services or supplies incidental to such lease before assumption of such lease unless the lessor is compensated

under the terms of such lease for any services and supplies provided under such lease before assumption of such lease.

"(c) The trustee may not assume or assign any executory contract or unexpired lease of the debtor, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties, if—

"(1)(A) applicable law excuses a party, other than the debtor, to such contract or lease from accepting performance from or rendering performance to the trustee or an assignee of such contract or lease, whether or not such contract or lease prohibits or restricts assignment of rights or delegation of duties; and

"(B) such party does not consent to such assumption or assignment; or

"(2) such contract is a contract to make a loan, or extend other debt financing or financial accommodations, to or for the benefit of the debtor, or to issue a security of the debtor; or

"(3) such contract or lease has been terminated under State law prior to the order for relief.

"(d)(1) In all cases under this title, if the trustee does not assume or reject an executory contract or unexpired lease of the debtor within 60 days after the order for relief, or within such additional time as the court, for cause, within such 60-day period, fixes, then such contract or lease is

deemed rejected; and, in the case of a lease, the court shall order the premises to be vacated immediately.

"(2) If an unexpired lease is assigned pursuant to this section, the lessor of the property may require a deposit or other security for the performance of the obligations under the lease substantially the same as would have been required by the landlord upon the initial leasing to a similar tenant.".

SEC. 3. Section 541 of title 11, United States Code, paragraph (b) thereof, is amended to read as follows:

"(b) Property of the estate does not include—

"(1) any power that the debtor may only exercise solely for the benefit of an entity other than the debtor; and

"(2) any property subject to a lease which has expired by virtue of its own terms without regard to the bankruptcy proceedings. In the case of property subject to a lease which has expired by virtue of its own terms, the lessor shall be entitled to enforce its rights to possession of the property subject to such lease without further order of the court and notwithstanding the provisions of section 362(a) of this title.".

ADDITIONAL MATERIAL FOR THE RECORD

STATEMENT FOR THE RECORD

OF THE NATIONAL RETAIL MERCHANTS ASSOCIATION

ON S. 2297

THE SHOPPING CENTER PROTECTIONS IMPROVEMENTS ACT OF 1982

INTRODUCTION

The National Retail Merchants Association (NRMA) appreciates this opportunity to present the views of the retailing industry on S. 2297, The Shopping Center Protections Improvements Act of 1982.

By way of background, NRMA is a national nonprofit voluntary trade association of over 3,500 members who operate more than 35,000 retail outlets. NRMA's members account for approximately $100 billion in sales annually, and they range in size from the largest department stores to small specialty shops. A substantial number of NRMA's members are tenants in shopping centers.

BACKGROUND

Shopping center tenants generally operate under long-term leases. The success of one is tied to the success of all. Problems in the operation of a shopping center must be remedied; they cannot be avoided by the tenants. Many shopping center tenants are family owned and operated businesses, with only one location. They are obligated under their lease to remain in that shopping center, tied to an interdependent relationship with other tenants. For this reason, there are reciprocal lease agreements which require, for example, that all stores be operated for a minimum number of hours each day, that certain business activities be carried on and others not be carried on, that all of the tenants advertise in certain ways to draw customers to their stores and, therefore, to all of the other stores.

In the Bankruptcy Reform Act of 1978 (the Code), Congress made unenforceable lease provisions which had protected solvent shopping center tenants from adverse effects of the bankruptcy of another shopping center tenant. These provisions had allowed shopping center landlords to regain control of the debtor's space so that it could be quickly re-leased to an operating tenant contributing to the tenant mix.

However, Congress recognized that solvent shopping center tenants needed and deserved protection from store closings and disruption of the tenant mix. Accord-

ingly, specific protections for nonbankrupt shopping center tenants were included in the Code. Unfortunately, in practice these protections have been ineffective. As a result, nonbankrupt shopping center tenants have been unnecessarily and unjustifiably injured by the administration of the estates of bankrupt tenants.

The purpose of this legislation is to make these protections effective. Two important changes in the Code would improve the protections for shopping center tenants. These are provisions which would: (1) reduce the time a store might be closed by requiring the trustee to decide within 60 days whether to approve or reject a lease, unless additional time is granted; and (2) prevent a trustee from assigning a lease to a business in violation of a use clause or from disrupting the shopping center's tenant mix.

The NRMA strongly supports this legislation because the current operation of the Bankruptcy Code poses the risk of serious economic harm and, perhaps, business failure to the solvent tenants of a shopping center that experience the bankruptcy of a tenant.

The closing of even a single store in a shopping center has the potential for dramatically affecting all other retail tenants by reducing their revenues and increasing their costs. Revenues are reduced because the closing of a store in a shopping center, especially a major store, reduces the traffic flow through the shopping center. In a regional shopping center with more than one major tenant, the reduction in traffic can have a negative effect on all of the tenants. This damage often is even more serious for the stores adjacent to the unoccupied space. In strip centers with only one major tenant, the closing of such a tenant generally has a substantial damaging effect on all of the stores.

The closing of a major tenant also can substantially increase the costs of the other tenants. Many shopping center leases today provide for pro rata payment of common area costs on the basis of percentage of leased space. The closing of a major tenant will substantially reduce the amount of leased space, thus increasing the percentage of all remaining tenants. This will cause their common area charge to be increased on a pro rata basis.

Another serious problem for shopping center tenants caused by the Code relates to the assignment of a lease to a business which does not conform to the use clause of the lease. Such an assignment, expecially in the case of a major store, can affect the other tenants much in the same way as the closing of the store. For example, in a small strip center, the assignment of the lease of grocery

store anchor to a store in another business with less drawing power would reduce the traffic of all of the other shopping center tenants.

In addition to this general depressive effect on customer traffic to the entire shopping center, stores adjacent to or in the same line of business as the assignee may also be severely impacted. The replacement of even a small store with high customer attraction power, such as a women's wear store, by another business which generates less traffic would have an adverse effect on the adjacent stores. A larger number of satellite stores adjacent to a closed department store or other major tenant in a mall would be similarly impacted.

In addition, changes in the business use of even small tenants can have a severe impact on competing businesses. For example, in a shopping center with three men's wear stores and three women's wear stores, the assignment of a women's wear store lease to a fourth men's wear store could seriously disadvantage the existing men's wear stores both by oversaturating the supply of men's clothing in that shopping center and by providing the assignee with an unfair competitive advantage.

Shopping center developers design a tenant mix that has the widest appeal to the potential trade area of a shopping center and, in so doing, determine the optimum number of each category and subcategory of merchant for their shopping centers. Adding a fourth men's wear store in this example would increase the number of men's wear stores by one-third. Such a substantial increase might so reduce the sales of the other stores as to make them unprofitable. It should be noted that many small shopping center tenants are locally owned and operated small businesses which, especially in these difficult economic times, may not survive such a situation.

The assignee store could additionally be given a competitive advantage over the three existing stores if the rental payments under its assigned women's wear store lease were lower than those of the other men's wear stores. Shopping center landlords generally charge the same rent of all stores competing with one another. Accordingly, it would be typical for all of the existing men's wear stores to be paying equivalent rents. However, women's wear stores would usually be charged a lower rent because of their drawing power. In such a case, the assignment of a women's wear store lease — at the lower women's wear store rental rate — to a men's wear store would give the assignee men's wear store a lower overhead.

Such a situation obviously is unfair to the existing tenants. Indeed, the

possibility of such an outcome makes a lease of shopping center space less valuable than would otherwise be the case.

In addition, the adverse effects of the closing or improper assignment of shopping center space may be greatly amplified by a "domino effect": the decrease in shopping center traffic caused by the closing or misassignment of a major tenant, especially during a recession, could cause the insolvency of other tenants. Should this occur, the effect on remaining tenants would be cumulative, and could result in the destruction of an entire shopping center and all of its merchants.

Moreover, either the closing of a store in a shopping center or the assignment of shopping center space to an assignee not in conformance with the use clause has an adverse impact not only on the other tenants in that shopping center but also on the workers they employ and the consumers they serve. Decreased traffic and sales volume reduce the need for employees, and decreased profits reduce the ability to pay such employees. Decreased sales volumes also make it difficult for retailers to sell at lower prices which volume selling permits. Thus, costs to the consumer may be increased as a result of the misoperation of the Bankrutcy Code.

CONCLUSION

The essence of the problem created for NRMA's members by the Bankruptcy Code is this: the closing of a shopping center store for an extended period of time or the assignment of a shopping center lease to a business which does not conform to the use clause of that lease — especially where either of these situations occurs in the case of a major tenant — hurts the business of all of the other tenants of that shopping center.

Under the Code, all reciprocal lease agreements may be abrogated by the trustee or debtor-in possession. The only way to solve the resulting problems is to change the Bankruptcy Code. There is nothing that the solvent tenants of a shopping center or the landlord can do to avoid financial hardship or disaster as a result of the breach by a debtor of these fundamental lease agreements. Indeed, the solvent tenants have no voice at all in the bankruptcy proceedings of another tenant.

Only the Congress can solve this problem which was created by the 1978 Act. The members of the NRMA strongly urge Congress to do so by swiftly enacting S. 2297 into law.

NRMA appreciates the opportunity to present the views of retailing on this important issue.

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